ABSTRACT

INTERNATIONAL AFFAIRS AND DEVELOPMENT

MSEKA, CHIKONDI O. B.A. McGill University, 1995

THE IMPACT OF FOREIGN DIRECT INVESTMENT ON THE ECONOMIC GROWTH AND DEVELOPMENT OF SUB-SAHARAN AFRICAN COUNTRIES

Advisors: Professor Cedric Grant, Professor T. Christopher Jespersen, and Professor Bernice de Gannes Scott

Thesis dated July, 1998

This study examines the social and economic effects of multinational corporations (MNCs), the main purveyors of foreign direct investment (FDI), on the countries of sub-Saharan Africa.

The study is based on the rift in empirical and theoretical findings concerning the actual effects of multinational presence in a developing country. On one hand, those who believe in the efficiency of MNCs in bringing about global development have produced studies and theories to support their view of multinationals as the "great equalizers among nations." On the other hand, those in disagreement with this view of the multinational have also produced studies and theories, which contend that the MNC has adverse effects on political and economic sovereignty and the fulfillment of basic needs in developing economies.

A regression analysis was used to investigate the effects of foreign direct investment (FDI), foreign aid (ODA) and political stability (PS) on the economic growth and economic development of thirty sub-Saharan African countries during two time periods: 1980-1989 and 1990-1995. Foreign aid and political stability were also used in the study due to the fact that both have been known to affect the direction of growth and

development. The time periods were chosen to analyze the effects of the end of the Cold War (1989) on sub-Saharan African countries.

The researcher found that political stability had the most significant impact on economic growth in period 2 and economic development in both time periods.

The conclusions drawn from the findings suggest that the small amount of foreign investment that sub-Saharan Africa receives probably accounts for its insignificant effects on economic growth and development. They also suggest that corruption concerning the misuse of foreign aid probably accounts for the insignificant effects that foreign aid had on economic growth and economic growth and development.

THE IMPACT OF FOREIGN DIRECT INVESTMENT ON THE ECONOMIC GROWTH AND DEVELOPMENT OF SUB-SAHARAN AFRICAN COUNTRIES

A THESIS

SUBMITTED TO THE FACULTY OF CLARK ATLANTA UNIVERSITY

IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR

THE DEGREE OF MASTER OF ARTS

BY

CHIKONDI OLUREMI MSEKA

SCHOOL OF INTERNATIONAL AFFAIRS AND DEVELOPMENT

ATLANTA, GEORGIA

JULY 1998

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ACKNOWLEDGEMENTS

For their patience and understanding, I would like to, first and foremost, thank my parents, Dr. and Mrs. Leonard and Ayodele Mseka. Their love and guidance have prepared me for many of life's goals and have allowed me to become the person I am today. Next, I would like to thank my sister, Adedayo Mseka, who never hesitated to spare time to listen and converse about several issues which concerned me during the course of my research. Karen Livingtone and Tanya Paxton, two of my oldest and dearest friends, have also been invaluable to me during the writing of this thesis. I would like to express my sincere gratitude for their constructive criticism, innovative suggestions and technical assistance. Dr. Cedric Grant, Dr. T. Christopher Jespersen, and Dr. Bernice Scott, my thesis committee members: thank you very much for your support and encouragement throughout the entire International Affairs program, and especially during the creation of this thesis. Academically and professionally, you are examples of what I aspire to be in the field of international affairs and development. I would also like to thank Dean Herschelle Challenor and Dr. Mustafah Dhada for providing the dynamic academic environment in which I learned about the significance of post-Cold War relations to the survival of the developing world. In closing, I would like to thank my friends and the administrative staff at the School of International Affairs and Development, with whom I exchanged the thoughts and ideas which prompted me to pursue my study of this particular facet of the international economic system.

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ABBREVIATIONS

CIA	Central Intelligence Agency
CIPEC	Council of Copper Exporting Countries
CPI	Consumer Price Index
ED	Economic Development
EDA	Economic Development Act
ECIL	Electronics Corporation of India Limited
EG	Economic Growth
EPZ	Export Protection Zone
FA	Foreign Aid
FATF	Financial Action Task Force
FDI	Foreign Direct Investment
FPI	Foreign Private Investment
GATT	General Agreement on Trade and Tariffs
GDP	Gross Domestic Product
GNP	Gross National Product
GM	General Motors
HDI	Human Development Index
HQM	High Quality Manpower

ABBREVIATIONS (Continued)

IBM	International Business Machines
ICL	International Computers Limited
ITT	International Telephone and Telegraph
ICOR	Incremental Capital-Output Ratio
LDC	Lesser Developed Country
MNC	Multinational Corporation
NIC	Newly Industrializing Country
OPEC	Organization of Petrol Exporting Countries
PS	Political Stability
ODA	Official Development Assistance
OECD	Organization of Economic Cooperation and Development
ONUC	United Nations Operations in the Congo
SIDS	Small Island Developing States
TCC	Transnational Capitalist Class
UN	United Nations
UNCTAD	United Nations Commission on Trade and Development
WTO	World Trade Organization
UMHK	l'Union Minière du Haute Katanga

CHAPTER I

INTRODUCTION

"Globalization" is the buzzword of the nineties. For those who have long awaited its arrival, it is symbolic of a more integrated world—one in which ideas and thoughts are shared by various nations and cultures for the betterment of humankind. In the seventies, Richard J. Barnet and Ronald E. Müller wrote of a world fraught by war and poverty, and the apparent absence of national pride and conventional patriotism.[1] These problems still plague the international community, and a loss of faith continues to transcend the world's numerous ideologies. This is what makes globalization so appealing. The word alone connotes unity and progress during a time when these two phenomena appear to be most unattainable.

By definition, globalization is the linkage of all aspects of a nation's economy—the industries, service sectors, levels of income and employment, and living standards—to the economies of its trading partners.[2] This interdependence facilitates the transfer of goods and services, labor, investment funds and technology. It also aids in the establishment of business enterprise on a global level. As far as the data are concerned,

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[1] Richard J. Barnet and Ronald E. Müller, *Global Reach: The Power of Multinational Corporations* (New York: Simon and Schuster, 1974), 65.

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the advent of globalization appears to have yielded some positive results. For instance, the growth in the telecommunications industry has not only brought poor countries into closer contact with world commercial centers and, more importantly, each other, but it has also had a tremendous impact on the international economic system.[3] Regional economic integration movements and other trade arrangements have significantly contributed to the increase in world trade, which has risen from total exports of US$308 billion to US$3.55 trillion between 1950 to 1992.[4] Telecommunications has also been a driving force in the creation of corporate alliance and consolidation.[5] Partially, as a result of this improvement in communications, foreign direct investment flows have increased from US$77 billion in the period between 1983 and 1987 to US$318 billion in 1995, a growth rate which is three times faster than the growth of world trade.[6]

Multinational corporations (MNCs), the main purveyors of foreign direct investment, have essentially spearheaded the process of globalization. MNCs became active forces in international trade in the late sixties and early seventies. Since that time, they have managed to obtain control of 70% of world trade, making them some of the

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[5] Grieder, 182.

[6] International Finance Corporation, *Lessons of Experience: Foreign Direct Investment* (Washington, DC: Library of Congress Publication, 1997), 5.

most important players in the international economic arena.[7]

The success of MNCs presents a great dilemma to the world system. In terms of economic growth, the increasing importance of MNCs in the future of the world economy is very good news. The post-World War II era has already been christened as the most successful period in international economic history.[8] Having played a significant role in this success, MNCs have achieved rates of capital accumulation once only dreamt about by various financial tycoons.

In terms of social development, however, the growth in the power of the MNC also brings with it a hint of despair. David C. Korten states that this day and age has witnessed the invention of the jet airplane, the fax machine, and the microwave oven; more than a billion people enjoy the abundance of affluence; and most importantly, there exists the knowledge and the technical capacity to end poverty, war and disease.[9]

Unfortunately, the same societies that have achieved these feats are suffering from a variety of social and economic ills. On a daily basis, the citizens of some of the most prosperous societies are experiencing high levels of unemployment, falling real wages, greater dependence on temporary, unsecured jobs, and uncertainty about their financial and social futures.[10] Corporate competition for natural resources has marginalized the

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[7] Ibid., 124; Paul Kennedy, *Preparing for the Twenty-First Century* (New York: Vintage Books, 1993), 50.

[8] Barnet and Müller, 123.

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incomes of those who depend on agricultural production.[11] Lastly, there has been an increase in violent crimes and the number of refugees. In essence, what Korten is describing is the proliferation of a three-fold human crisis that is plaguing the developed world: (1) deepening poverty, (2) social disintegration, and (3) environmental destruction.[12]

These realities debunk the notion that the wealth of multinationals trickles down and eventually reaches the masses. Some of the oldest and richest multinationals are headquartered in the United States (e.g. Coca-Cola, General Motors, Microsoft and PepsiCo) and their wealth has yet to completely alleviate the country's social problems. As evidenced by the MNC's relentless pursuit of capital accumulation, and the resulting social upheaval, the corporation's mere existence is both unapologetic and uncompromising in the face of human interests.

Ted C. Lewellen quotes Sklar who claims that those who adhere to the notion of the nation state as the primary unit of international affairs are misinformed.[13] In the current international arena, MNCs are the primary units of power.[14] What does this mean for the future welfare of developing countries, whose social and economic survival

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[10] Ibid., 19.

[11] Ibid.

[12] Ibid., 18.

[13] Ted C. Lewellen, "Between Debt and the Deep Blue Sea: The Third World in the International Economy," in *Dependency and Development: An Introduction to the Third World* (London: Bergin & Garvey, 1995), 110.

hinges on the benevolence or malevolence of these multinational organizations? While MNCs enjoy the fruits of their success, 1.3 billion people are attempting to eke out an existence on less than a dollar a day.[15] Since, the decisions of some of the world's biggest corporations have a greater impact on the lives of citizens of developing countries than do the policies of their own governments, it seems as though these organizations have significantly contributed to this state of affairs.[16]

Peter D. Sutherland and John W. Sewell maintain that one of the fundamental challenges to globalization is to make sure that its benefits reach all countries and all peoples.[17] Data on social development reveal that globalization has failed in this area and apparently without remorse. Paul Kennedy states that without the constraints of the Cold War, MNCs will continue to take advantage of the emerging free markets for their own gain.[18] If developed countries have not been able to fully benefit from the MNC, how are developing countries supposed to do the same? More specifically, where does this leave sub-Saharan Africa? With extremely low rates of life expectancy and educational

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[14] Ibid.

[15] World Bank, *World Development Indicators, 1997* (Washington, DC: International Bank for Reconstruction and Development/THE WORLD BANK, 1997), 22.

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attainment, sub-Saharan Africa rivals South Asia as the world's poorest region.[19] How can the countries of this region compete with corporations that will inevitably undermine the ability of their nation-states to provide basic necessities for their citizens?

Herein lie the origins of this research effort. A true test of the efficacy of the MNC in sharing the world's wealth and the success of globalization as a whole is to analyze the development of regions such as sub-Saharan Africa. This project poses pertinent, but seldom-asked questions: Has foreign direct investment positively contributed to the social and economic development of sub-Saharan Africa? Or, are their profits indicative of "pariah-type" activities that are impoverishing some of the most resource-rich countries in the world?[20] Should other factors be blamed? Perhaps foreign aid or political instability is as much to blame or even more so? These questions will be addressed and analyzed in the course of this study.

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[19] Michael P. Todaro, *Economic Development,* Fifth Edition (London: Longman, 1994), 146.

[20] The reference to a multinational as a "pariah" is an analogy to K.J. Holsti's notion of a "pariah state". In *International Politics: A Framework for Analysis* (Englewood Cliffs: New Jersey, 1992), 179-319, Holsti claims that there are pariah states that violate the established norms and expectations in the international system by participating in acts such as terrorism and other human rights abuses. Terrorism interferes with a nation's right to function in an environment conducive to its pursuit of self-determination. Examples of such states are Communist China in the fifties and Uganda in the sixties. The reference to the actions of multinationals as "pariah-like" is in congruence with this mode of thinking. Those who object to the presence of multinationals in developing countries often refer to MNCs as pariah-like organizations whose actions hinder a nation's ability to practice social and economic sovereignty.

Statement of the Problem

This study proposes to establish the extent to which foreign direct investment is responsible for the social and economic decline of the countries of sub-Saharan Africa. The bulk of the literature reviewed for this study implicates foreign direct investment, or more specifically, the multinational corporation, as having an adverse effect on the course of the region's social and economic development. This may not be the case, statistically, however. It is the duty of research efforts, like this one, to take logical and analytical steps toward answering the question.

The Sub-problems

The first sub-problem deals with whether or not foreign aid has had an effect on the region's development path. If foreign aid has had a positive effect on the region's development path, then it might offset the negative effects of foreign direct investment. Conversely, if it has had a negative impact, it might be the cause, more so than foreign direct investment, of the region's development problems.

The second sub-problem is to uncover the effect of political instability on sub-Saharan Africa's development. Various authors have found that political instability, in and of itself, can set off a chain reaction that inevitably affects a nation's social and economic prosperity.[21]

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[21] Kwabena Gyimah-Brempong and Thomas L. Traynor, "Political Instability and Savings in Less Developing Countries: Evidence from Sub-Saharan Africa," *Journal of Development Studies* 32, no. 5 (June 1996): 695-714.

The Hypotheses

The first hypothesis is that foreign direct investment has had a negative impact on the region's economic growth and development.

Consequently, the second hypothesis is that foreign aid has had less of an impact on the region's economic growth and development.

The third hypothesis is that political stability, or a lack thereof, has had less of an impact on economic growth and development than has foreign direct investment.

The Delimitations

This project will study the effects of foreign direct investment on 30 of the 48 sub-Saharan African countries. (See Appendix One)

Political instability will be measured in terms of the presence of violent and nonviolent political events that disrupt the political system. Both types of instability have been found to negatively affect the amount of savings that a country engages in, and therefore, the country's development pace.[22]

This study will compare and contrast two specific time periods: 1980-1989 and 1990-1995. These time periods were chosen to compare and contrast the lot of sub-Saharan African countries during and after the Cold War. The next section will demonstrate that since the end of the Cold War (1989), there has been a decrease in foreign aid and an increase in foreign direct investment to sub-Saharan Africa. By

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[22] Ibid.

comparing and contrasting both time periods, one can investigate the effects of this trend on sub-Saharan African growth and development.

Definition of Terms

"Foreign direct investment" is defined as the amount of financing from a foreign owner who is directly involved in the management of the firm or corporation.[23]

"Economic growth" is the increase in the productive capacity of an economy, which experiences an increase in its national income.[24]

In contrast, "economic development" is conceptualized as an increase in the social well being of a nation's population. Overall, well being involves the improvement in various quality of life indicators: life expectancy, infant mortality, mean years of schooling, etc.[25]

Global corporate expansion over the years has fostered some controversy as to what term should be used to define the global enterprise. Even the United Nations Commission on Transnational Corporations has been unable to settle on a definition.[26]

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[23] International Finance Corporation/Foreign Investment Advisory Service, "The Role of FDI in Developing Countries," in *Foreign Direct Investment: Lessons of Experience, Number 5* (Washington, DC: World Bank, 1997), 9.

[24] Todaro, 672.

[25] Jan S. Hogendorn, *Economic Development,* Third Edition (New York, New York: HarperCollins College Publishers, Inc., 1996), 37.

[26] Rhys Jenkins, "Transnational Corporations: Significance and Growth," in *Transnational Corporations and Uneven Development* (London: Methuen, 1987), 1.

The most interesting division exists between those who prefer to define this particular type of international organization with the term "multinational corporation," and those who favor the term "transnational corporation." The two terms are different due to the fact that "multinational" simply refers to a firm based in one country with subsidiaries in more than one location outside its home country.[27] Some view this term as erroneous because it implies multinational ownership of the firm. There is a continual lack of indigenous presence in an international corporation's managerial and ownership structures. "Transnational" corporations are said to be owned by investors from a variety of countries, even though the firms are headquartered in only one country.[28]

Endless interpretations of this enterprise leave researchers to rely on preference or to use the terms interchangeably. This project chooses the term "multinational corporation" and defines it according to David Korten's interpretation:

> A multinational corporation takes on many national identities, maintaining relatively autonomous production and sales facilities in individual countries, establishing local roots and presenting itself in each locality as a good local citizen.[29]

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[27] F.E.I. Hamilton, "The Multinationals: Spearhead or Spectre?" in *Multinational Corporations and the Third World,* eds. C.J. Dixon, D.Drakakis-Smith, and H.D. Watts (London: Croom Helm, 1986), 3.

[28] Korten, 125.

Assumptions

The first assumption is that foreign direct investment has played a significant role in the region's social and economic development.

The second assumption is that the respective effects of foreign aid and political stability have been less significant.

The Importance of the Study

This study is important because it examines African development in light of the end of the Cold War. Since 1989, most of the countries in the region have lost their importance in global affairs because they are no longer considered part of the containment strategies of Western powers. In other words, the end of the Cold War has eliminated their role as theaters for the East-West rivalry. Angola's affiliation with the Soviet Union and Zaire's ties with the West have been all but forgotten in the rush to establish open markets and democracies in the wake of the Iron Curtain's collapse. The decline in foreign aid to sub-Saharan Africa is a testament to this statement. Official Development Assistance (ODA) flows to the former Soviet Union and Eastern European countries jumped from 1.4% in 1990 to 7.1% in 1992.[30] This increase was accompanied by a small but significant decline in Africa's share of ODA in the same time period

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[29] Ibid., 125.

[30] World Bank, *World Debt Tables: External Finance for Developing Countries, Volume 1, Analysis and Summary Tables* (Washington, DC: The International Bank for Reconstruction and Development/The World Bank, 1993), 13.

(37.1% to 36.3%).[31]

Michael Todaro states that developing countries regard this turn of events as the "crowding-out phenomenon" because the increasing need for foreign assistance in the former Soviet bloc appears to be overshadowing their needs.[32] According to Stephan Schmidheiny and Federico Zorraquín this trend will continue.[33] Therefore, one of the main sources of badly needed foreign capital is slowly but surely becoming foreign direct investment.

Fortunately, the decrease in ODA has been accompanied by an increase in foreign direct investment. Jean-Louis Buchet refers to this phenomenon as the "silent revolution."[34] From 1990 to 1996, private capital flows to the developing world jumped from $44.4 million to $243 million.[35] Admittedly, most of these flows have gone to countries in Asia and Latin America. However, this capital can still be quite beneficial to the development efforts of all developing countries, especially sub-Saharan Africa. Therefore, uncovering the negative effects of MNC activity in the region can ultimately

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[31] Ibid.

[32] Todaro, 646.

[33] Schmidheiny, Stephan and Federico Zorraquín, *Financing Change: The Financial Community, Eco-efficiency, and Sustainable Development* (London: The MIT Press, 1996), 6, 31.

[34] Jean-Louis Buchet, "La Rėvolution Silencieuse," *Jeune Afrique* 1893 (April 16-22, 1997): 42.

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allow sub-Saharan African countries to participate in a more equitable international economic environment.

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The second sub-problem is to uncover the effect of political instability on sub-Saharan Africa's development. Various authors have found that political instability, in and of itself, can set off a chain reaction that inevitably affects a nation's social and economic prosperity.[21]

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[21] Kwabena Gyimah-Brempong and Thomas L. Traynor, "Political Instability and Savings in Less Developing Countries: Evidence from Sub-Saharan Africa," *Journal of Development Studies* 32, no. 5 (June 1996): 695-714.

The Hypotheses

The first hypothesis is that foreign direct investment has had a negative impact on the region's economic growth and development.

Consequently, the second hypothesis is that foreign aid has had less of an impact on the region's economic growth and development.

The third hypothesis is that political stability, or a lack thereof, has had less of an impact on economic growth and development than has foreign direct investment.

The Delimitations

This project will study the effects of foreign direct investment on 30 of the 48 sub-Saharan African countries. (See Appendix One)

Political instability will be measured in terms of the presence of violent and nonviolent political events that disrupt the political system. Both types of instability have been found to negatively affect the amount of savings that a country engages in, and therefore, the country's development pace.[22]

This study will compare and contrast two specific time periods: 1980-1989 and 1990-1995. These time periods were chosen to compare and contrast the lot of sub-Saharan African countries during and after the Cold War. The next section will demonstrate that since the end of the Cold War (1989), there has been a decrease in foreign aid and an increase in foreign direct investment to sub-Saharan Africa. By

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[22] Ibid.

comparing and contrasting both time periods, one can investigate the effects of this trend on sub-Saharan African growth and development.

Definition of Terms

"Foreign direct investment" is defined as the amount of financing from a foreign owner who is directly involved in the management of the firm or corporation.[23]

"Economic growth" is the increase in the productive capacity of an economy, which experiences an increase in its national income.[24]

In contrast, "economic development" is conceptualized as an increase in the social well being of a nation's population. Overall, well being involves the improvement in various quality of life indicators: life expectancy, infant mortality, mean years of schooling, etc.[25]

Global corporate expansion over the years has fostered some controversy as to what term should be used to define the global enterprise. Even the United Nations Commission on Transnational Corporations has been unable to settle on a definition.[26]

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[23] International Finance Corporation/Foreign Investment Advisory Service, "The Role of FDI in Developing Countries," in *Foreign Direct Investment: Lessons of Experience, Number 5* (Washington, DC: World Bank, 1997), 9.

[24] Todaro, 672.

[25] Jan S. Hogendorn, *Economic Development,* Third Edition (New York, New York: HarperCollins College Publishers, Inc., 1996), 37.

[26] Rhys Jenkins, "Transnational Corporations: Significance and Growth," in *Transnational Corporations and Uneven Development* (London: Methuen, 1987), 1.

The most interesting division exists between those who prefer to define this particular type of international organization with the term "multinational corporation," and those who favor the term "transnational corporation." The two terms are different due to the fact that "multinational" simply refers to a firm based in one country with subsidiaries in more than one location outside its home country.[27] Some view this term as erroneous because it implies multinational ownership of the firm. There is a continual lack of indigenous presence in an international corporation's managerial and ownership structures. "Transnational" corporations are said to be owned by investors from a variety of countries, even though the firms are headquartered in only one country.[28]

Endless interpretations of this enterprise leave researchers to rely on preference or to use the terms interchangeably. This project chooses the term "multinational corporation" and defines it according to David Korten's interpretation:

> A multinational corporation takes on many national identities, maintaining relatively autonomous production and sales facilities in individual countries, establishing local roots and presenting itself in each locality as a good local citizen.[29]

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[27] F.E.I. Hamilton, "The Multinationals: Spearhead or Spectre?" in *Multinational Corporations and the Third World,* eds. C.J. Dixon, D.Drakakis-Smith, and H.D. Watts (London: Croom Helm, 1986), 3.

[28] Korten, 125.

Assumptions

The first assumption is that foreign direct investment has played a significant role in the region's social and economic development.

The second assumption is that the respective effects of foreign aid and political stability have been less significant.

The Importance of the Study

This study is important because it examines African development in light of the end of the Cold War. Since 1989, most of the countries in the region have lost their importance in global affairs because they are no longer considered part of the containment strategies of Western powers. In other words, the end of the Cold War has eliminated their role as theaters for the East-West rivalry. Angola's affiliation with the Soviet Union and Zaire's ties with the West have been all but forgotten in the rush to establish open markets and democracies in the wake of the Iron Curtain's collapse. The decline in foreign aid to sub-Saharan Africa is a testament to this statement. Official Development Assistance (ODA) flows to the former Soviet Union and Eastern European countries jumped from 1.4% in 1990 to 7.1% in 1992.[30] This increase was accompanied by a small but significant decline in Africa's share of ODA in the same time period

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[29] Ibid., 125.

[30] World Bank, *World Debt Tables: External Finance for Developing Countries, Volume 1, Analysis and Summary Tables* (Washington, DC: The International Bank for Reconstruction and Development/The World Bank, 1993), 13.

(37.1% to 36.3%).[31]

Michael Todaro states that developing countries regard this turn of events as the "crowding-out phenomenon" because the increasing need for foreign assistance in the former Soviet bloc appears to be overshadowing their needs.[32] According to Stephan Schmidheiny and Federico Zorraquín this trend will continue.[33] Therefore, one of the main sources of badly needed foreign capital is slowly but surely becoming foreign direct investment.

Fortunately, the decrease in ODA has been accompanied by an increase in foreign direct investment. Jean-Louis Buchet refers to this phenomenon as the "silent revolution."[34] From 1990 to 1996, private capital flows to the developing world jumped from $44.4 million to $243 million.[35] Admittedly, most of these flows have gone to countries in Asia and Latin America. However, this capital can still be quite beneficial to the development efforts of all developing countries, especially sub-Saharan Africa. Therefore, uncovering the negative effects of MNC activity in the region can ultimately

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[31] Ibid.

[32] Todaro, 646.

[33] Schmidheiny, Stephan and Federico Zorraquín, *Financing Change: The Financial Community, Eco-efficiency, and Sustainable Development* (London: The MIT Press, 1996), 6, 31.

[34] Jean-Louis Buchet, "La Révolution Silencieuse," *Jeune Afrique* 1893 (April 16-22, 1997): 42.

[35] Ibid.

allow sub-Saharan African countries to participate in a more equitable international economic environment.

CHAPTER II

LITERATURE REVIEW

Introduction

This section provides a historical and contemporary look at sub-Saharan Africa's social and economic problems. It also analyzes the MNC from the same perspectives, highlighting (1) the MNC's role in the region's development path and (2) the quintessential debate between the proponents and opponents of foreign direct investment. The debate sets the stage for the discussion of a variety of issues, mainly the relationship between foreign direct investment and sustainable development and the predicament of small island developing states and their dependence on foreign direct investment for economic survival.

Africa's Plight

> The world system, right from the era of the slave trade through colonialism to contemporary neo-colonialism has never favored Africa. The region has historically been marginal to the outside world in terms of cheap labor, raw materials and a dumping ground for out-dated and second rate products...Africans were never perceived as capable of handling their own affairs.[1]

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[1] Julius O. Ihonvbere, "Between Reform and Disaster: Options for Sub-Saharan Africa in the Emerging Global Order," in *Conflicts and New Departures in World Society*, eds. Volker Bornschier and Peter Lengyel (New Brunswick, New Jersey:

This statement serves both as an explanation of the plight of the African continent today and as the *raison d'être* of this study. Nowhere is the development debate more contentious than on the African continent, or for the purpose of this research, the region of sub-Saharan Africa. Decades of foreign exploitation, or what Samir Amin refers to as the "white peril"[2] have left professionals and scholars alike scrambling for explanations and solutions to what appears to be the one of the most catastrophic development disasters of recent times.

The fifties and sixties were a time of hope and promise for many of these countries. They had answered Kwame Nkrumah's call to, "Seek ye first the political kingdom," and through import substitution and export promotion development strategies, were poised to use their abundant resources to their fullest potential. Unfortunately, the remnants of colonialism, the effects of two oil crises, and the ensuing Structural Adjustment Programs (SAPs) shattered dreams of economic development. Paul Kennedy's *Preparing for the Twenty-First Century* states that these factors have rendered sub-Saharan Africa, "...a human and environmental disaster area,...peripheral to the rest of the world..."[3]

Since independence in the 1960's, Africa's population has risen from 281 million

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Transaction Publishers, 1994), 299.

[2] Samir Amin, *Delinking: Toward a Polycentric World* (London: Zed Books, 1990), 143.

[3] Paul Kennedy, *Preparing for the Twenty-First Century* (New York: Vintage Books, 1993), 211.

to 647 million.[4] This growth has hampered the development of the continent because production in the agricultural and manufacturing sectors has not kept up to speed. Africa actually lost the ability to feed itself. In *Global Dreams: Imperial Corporations and the New World Order,* Richard Barnet and John Cavanagh report that in the seventies the world grain trade expanded by 60%, and the United States managed to corner four-fifths of the market.[5] The ever-growing American monopoly marginalized many Third World producers from the market, and for the first time in history, countries such as Somalia, Mozambique, Sierra Leone, and Angola became dependent on wheat, corn, and rice imports.[6] According to Kennedy, the continent still has to import 15 million tons of maize a year to meet minimum levels of food consumption.[7]

Kennedy goes on to report that skyrocketing debt has compounded the region's difficulties. Fueled by the desire to modernize their economies, many newly established sub-Saharan African nations borrowed large amounts of money for the construction of national airlines, electrification schemes, and telephone networks.[8] Unfortunately, many of these schemes were doomed to failure due to bureaucratic interference, unskilled

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[4] Ibid., 213.

[5] Richard J. Barnet and John Cavanagh, *Global Dreams: Imperial Corporations and the New World Order* (New York: Simon & Schuster, 1994), 252.

[6] Ibid.

[7] Kennedy, 215.

[8] Ibid., 214.

personnel, unrealistic planning, and inadequate basic facilities.[9] Sub-Saharan Africa's debt statistics are the manifestation of these development catastrophes. Michael Todaro has found that between 1975 and 1989, sub-Saharan Africa's total external debt increased from US$14.9 billion to US$113.8 billion.[10] Julius Ihovnbere states that by 1990, the region's debt was 102.3% of its GNP, which had declined at a rate of 1.7% annually during the previous decade.[11]

Hazel Johnson's work, *Dispelling the Myth of Globalization: The Case for Regionalization,* postulates that these figures partially explain why 33 of the 53 countries of the world with a per capita GNP of less than $500 are located in sub-Saharan Africa.[12] They are also said to explain why 70 out of every 100 Africans are destitute or on the verge of poverty, only one out of four Africans has access to clean water and adult literacy and life expectancy rates are at all time lows.[13] Lastly, her research suggests that these harsh realities suggest that some form of foreign exploitation is to blame for this state of affairs. How else can one explain such social and economic devastation in a region rich with many of the world's most precious metals and minerals (i.e. diamonds,

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[9] Ibid.

[10] Michael P. Todaro, *Economic Development,* Fifth Edition (London: Longman, 1994), 460.

[11] Ihonvbere, 300.

[12] Hazel Johnson, *Dispelling the Myth of Globalization: The Case for Regionalization* (New York: Praeger, 1991), 10.

[13] Ihonvbere, 300.

copper, gold, platinum, zinc, etc.)?

Dependency theorists have purported that ex-colonial powers and their exploitation of these resources are to blame for sub-Saharan Africa's problems. Ihonvbere states that the colonial experience left Africa with a corrupt, weak, fractionalized, and unproductive dominant class, an impotent and marginalized industrial sector with little or no linkages to other sectors of the economy, and bastardized educational, social, and cultural forms and traditions.[14]

Agbeko Katapu expounds on Ihonvbere's proclamations. In *Workable Strategies to End Africa's Poverty: Some Aspects of nation Management Economics,* he claims that the African elite that took over after independence misunderstood the meaning of development.[15] Katapu stipulates that Africa's elite appeared to be more concerned with what was going on in the North (i.e. Europe and the United States) than what was unfolding in their own backyards. They perceived development in terms of consumption: "...eating, drinking or enjoying whatever is produced in industrialized nations first, and letting production take care of itself later."[16]

As African countries were being turned into consumer societies, their prospects for developing strong social and economic infrastructures were becoming less and less of

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[14] Ibid., 297.

[15] Agbeko Katapu, "Misunderstanding of Development," in *Workable Strategies to End Africa's Poverty: Some Aspects of Nation Management Economics* (Syracuse, New York, 1986), 3.

[16] Ibid., 4.

a reality. By not concentrating on improving production, which would have placed the region in a better position to provide for itself, the elite placed a major road block in the way of Africa's industrialization—a factor which Katapu upholds as one of the major keys to the success of US and European economies.[17] One might think that the mindset of Africa's elite during, what many would argue, was the region's most promising period seems to have helped to solidify Africa's marginal position in the international economic system. Many authors believe that this position was partially cultivated and has been maintained by the activities of MNCs in the sub-Saharan African region.

Brief History of Multinationals in Sub-Saharan Africa

Louis Turner's research states that ever since the days of adventurers such as Cecil Rhodes, who incidentally had plans to paint the map of Africa red (British flag), sub-Saharan Africa has been viewed as fertile ground for the European market.[18] Increased urbanization in Europe and the United States produced a great demand for coffee, tea and cocoa from West Africa, diamonds from South Africa, and copper from the rest of southern Africa.[19] These and countless other commodities attracted the earliest MNCs to the region. Walter Rodney's *How Europe Underdeveloped Africa* concurs with Turner's observations. The need for palm oil in the production of soap led William Lever

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[17] Ibid., 7, 18.

[18] Louis Turner, *Multinationals and the Third World* (New York: Hill and Wang, 1973), 18.

[19] Ibid.

(soap magnate of the 1800's) and other businessmen into southern and western Africa as early as 1887.[20] Lever's company (Unilever) would later emerge as one of the biggest monopolies on the continent.[21]

Economic ventures in the continent since that time may have been profitable for European and American investors, but sub-Saharan African colonies, and later on nations, ultimately paid the price for European economic expansion. Several authors report that multinationals have acted independently and have been used by various governments to disrupt the region's political and economic systems for the sake of profit and foreign policy.

Turner's work reveals that the Belgian mining company, *l'Union Minière du Haute Katanga* (UMHK), maintained a stranglehold on the Zairian economy for almost seven decades.[22] UMHK was one of the companies that King Leopold II created just before he relinquished power of the Congo in 1906.[23] Since the company was far from the capital (Leopoldville) and situated in one of the richest provinces in the country (Katanga), UMHK businessmen were able to behave with a great deal of autonomy with respect to the central government. The company became the seat of power for what resembled a country inside another country. For example, UMHK paid $40 million in

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[20] Walter Rodney, *How Europe Underdeveloped Africa* (Washington, D.C.: Howard University Press, 1982), 181.

[21] Ibid., 182.

[22] Turner, 27.

[23] Ibid., 28.

taxes a year to the Katanganese province, not the central government in Leopoldville.[24]

By 1957, the year of the country's first democratic elections, UMHK had become the chief industrial producer in the country, and was reluctant to give up its comfortable position in the economy.[25] The company backed its own political candidate, Moise Tshombe, and won.[26] Encouraged by the excitement of victory and the potential economic and political power of the region, Tshombe and UMHK officials attempted to secede from Zaire—an uprising that was suppressed by General Mobutu Sese Seko and the United Nations Operation in the Congo (ONUC) in 1965.[27]

Tshombe's defeat marked the beginning of a long battle between the Zairian government and the owners of UMHK, Société Général.[28] The company repeatedly refused to announce increases in the price of copper and reportedly thwarted the government's attempts to obtain partial ownership of its holdings.[29] In the late sixties, the company was booted out of Zaire and quickly replaced with American, European and Japanese mining companies that were more willing to heed the country's nationalistic tendencies.[30]

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[24] Ibid., 29.

[25] Ibid., 29-30.

[26] Ibid., 30.

[27] Ibid.

[28] Ibid.

[29] Ibid.

Turner and Barnet and Müller assert that the Firestone company's history in sub-Saharan Africa is also quite sordid. It virtually bought the country of Liberia in order to have unlimited access to the nation's rubber supply.[31] Barnet and Müller state that in 1920 the company lent money to the bankrupt Liberian government.[32] This loan gave Firestone the privilege of shaping the economic environment to fit its needs. In exchange for the company's gesture, the Liberian government was obligated to acquire an American financial adviser and relinquish control of the only bank and the country's lucrative distributorships of American and European consumer goods.[33] Through its control of the national bank, Firestone had the power to increase the country's foreign debt.[34] The extent of Firestone's power in Liberia is further demonstrated by the fact that the company actually had the power to increase the price of rice, which is the staple of the Liberian diet.[35] Liberia's ties to the company were severed in 1952 when the country repaid the infamous Firestone loan.[36]

Western MNC activities in South Africa and the surrounding region also support

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[30] Ibid.

[31] Ibid., 25.

[32] Richard J. Barnet and Ronald E. Müller, *Global Reach: The Power of the Multinational Corporations* (New York: Simon and Schuster, 1974), 87.

[33] Ibid.

[34] Ibid.

[35] Turner, 26.

[36] Ibid.

the claim that multinationals in sub-Saharan Africa have had a less than pristine track record on the continent. *Inequality in Africa: Political Elites, Proletariat, Peasants and the Poor* by E. Wayne Nafziger describes several of the motives of MNCs in this part of the world.[37] He reports that between 1960 and 1985 half of Western MNC investment in Africa was located in South Africa.[38] This gave MNCs and the South African government the opportunity to engage in economic hegemony in southern Africa. The main goal of these two forces was to convert the rest of southern Africa into a guaranteed source of labor, markets and raw materials.[39] The evidence suggests that these aspirations proved successful. MNCs with subsidiaries in South Africa managed to control the banking systems in numerous southern African countries, neglect their manufacturing and mining industries, and invest the surplus in South Africa.[40]

In his article, "The Imperialist-Apartheid Alliance," William J. Pomeroy states that the objectives of MNCs in this part of the world were furthered by South Africa's value to the leading capitalist powers. In addition to its established position as a regional superpower, South Africa was of particular value to the US and European countries whose main interest was to curb Communist expansion.[41] South Africa's Cape sea route

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[37] E. Wayne Nafziger, *Inequality in Africa: Political Elites, Proletariat, Peasants and the Poor* (Cambridge: Cambridge University Press, 1988), 51-52.

[38] Ibid., 51.

[39] Ibid.

[40] Ibid.

[41] William J. Pomeroy, "The Imperialist-Apartheid Alliance," in *Apartheid,*

was a prime location to monitor the travel of Communist vessels to the Indian Ocean and Asia.[42]

South Africa was also financially valuable to Western politicians. The country is home to 86% of the world's platinum, 64% of its vanadium, 49% of its gold, 48% of its manganese, and a significant share of it's supply of uranium, tritium, and lithium.[43] Some of these metals can be used in the production of nuclear missiles and other forms of artillery.[44]

Pomeroy implies that these attributes led many Western powers to ignore the negative aspects of apartheid in order to achieve their political and economic goals. The oppression of all those not part of the white minority was basically seen as the price that had to be paid for Allied Security. As South Africa was being increasingly shunned by the international donor community, the US, Great Britain, Germany and France pumped money into the economy through other means. Beginning in the late fifties and early sixties, South Africa became a popular destination for foreign investment, loans and trade in sub-Saharan Africa and ultimately one of the last allies of imperialism.[45] British investments at this time totaled $2.5 billion, West Germany's investments equaled $280

Imperialism, and African Freedom (New York: International Publishers, 1986), 29.

[42] Ibid., 30.

[43] Ibid., 29.

[44] Ibid.

[45] Ibid., 27.

billion, and the US had invested $288 billion.[46] By 1984, sixty-five of the largest international firms in the world, most of which influenced the foreign policies of their respective host governments, had major stakes in the South African economy.[47]

The US interests in the country were reflected in the legislation passed in the late sixties. Henry Kissinger, National Security Advisor at the time, went against sanctions established by the United Nations and intensified US support for South Africa and the rest of white settler ruled southern Africa.[48] The result of this action was the National Security Council's memo NSSM-39 or the "Tar Baby Report."[49] This document legitimized the relations with South Africa on the grounds that African liberation movements were transitory and that white rule in South Africa should be preserved in order to maintain the stability needed to prohibit Communist intervention in African affairs.[50] The significant amount of foreign investment, in the form of arms contracts and other corporate endeavors, allowed South Africa to play this controversial role.[51]

Despite the end of apartheid, the MNC continues to play a veritable role in the political and economic affairs of the countries on the African continent. Russell

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[46] Ibid.

[47] Ibid.

[48] Ibid., 32.

[49] Ibid.

[50] Ibid.

[51] Ibid., 33.

Mokhiber and Andrew Wheat have pinpointed Royal Dutch Shell as one of the ten worst corporations because of its activities in Nigeria's Ogoni region.[52] For quite some time, Nigeria has been an important source of oil for Shell in that it accounts for 14% of Shell's worldwide production.[53] The importance of Nigeria's oil rich lands to Shell has supposedly prompted the company to ignore cries of political collaboration with Nigeria's military dictatorship and environmental pollution. Mokhiber and Wheat claim that multinationals such as Shell, which find themselves in close partnerships with corrupt regimes, often rationalize the relationship by adopting a "constructive engagement" policy that they claim benefits the masses and sets an example for the corrupt government itself.[54]

As evidenced by the social upheaval caused by Shell's operations in Ogoni lands, the constructive engagement policy has failed. Playwright and environmentalist Ken Saro-Wiwa led numerous protests to end almost a decade of environmental pollution, during which 1.6 million gallons of oil were spilled in Ogoni territory.[55] Since 1993, he and hundreds of others have reportedly been killed by factions inside the Nigerian government who are willing to undertake "ruthless military action" in order for "smooth

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[52] Russell Mokhiber and Andrew Wheat, "Shameless: 1995's 10 Worst Corporations," *Multinational Monitor* 16, no. 12 (December 1995): 10.

[53] Ibid.

[54] Ibid.

[55] Ibid.

economic activities to take place."[56]

The highly lucrative nature of foreign investment in sub-Saharan Africa and the rest of the developing world has aided in the proliferation of global enterprises similar to the ones just discussed to the point where the advent of the MNC can be truthfully characterized as a phenomenon.

The Growth and Power of the Multinational

David Korten's *When Corporations Rule the World* accuses MNCs of being the main proponents of corporate colonialism, preying on weak economies in pursuit of ever-growing profits and global empires.[57] Economic history and contemporary statistics reveal that they have been very successful in their profit-seeking goals. As stated in the introduction, over the past few decades, the MNC has experienced a growth in profits and dominance. F.E.I. Hamilton cites a study by J.H. Dunning, which offers an overview of the MNC phenomenon.[58]

After having enjoyed the success of their colonial ventures, MNCs experienced an economic downturn. Dunning states that foreign direct investment decreased significantly between 1914 and 1960. Two sets of factors were responsible. First of all,

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[56] Ibid.

[57] David C. Korten, *When Corporations Rule the World* (West Hartford, Connecticut: Kumarian Press, Inc., 1995), 28.

[58] F.E.I. Hamilton, "The Multinationals: Spearhead or Spectre?" in *Multinational Corporations and the Third World,* eds. C.J. Dixon, D. Drakakis-Smith, and H.D. Watts (London: Croom Helm, 1986), 1-24.

the worldwide economic recession in the 1920's, which resulted in the Great Depression in the US between 1929 and 1932, significantly restricted the volume of overseas exports in almost all industries.[59] Furthermore, sales revenues fell, over-capacity increased and sufficient profit rates disappeared. Economic nationalism worsened the lot of MNCs in the years to come. Governments insistent on making foreign investment a pivotal force in their development efforts subjected MNCs to higher taxes and sometimes demanded partial ownership in a foreign enterprise to ensure a portion of the profits.[60]

Dunning's study asserts that other factors contributed to the decline in foreign investment during the same time period. By adopting anti-trust policies, such as the Clayton Act of 1914 and the Cellar-Kefauver Act of 1950, the American government made giant strides in the effort to topple many of the monopolies and oligopolies in the electrical and chemical industries.[61] Dunning states that this probably reduced the ability of individual companies to set up operations abroad.

Finally, Dunning claims that three sets of factors led to the increase in MNC activity after 1960: (1) the rebirth of the economies of Western Europe and Japan, which opened up new markets for American companies, paved the way for the entry of New Industrializing Countries (NICs) and other developing countries into the trading game, and set the stage for Cold War arms dealings; (2) the liberalization of trade in the 1970's;

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[59] Ibid., 5.

[60] Ibid.

[61] Ibid.; Barnet and Cavanagh, 231.

(3) and the increase in technological innovations, which facilitated the collection, processing and transfer of information.[62]

MNCs have continued to experience phenomenal success since that period. *Sociology of the Global System* by Leslie Sklair demonstrates that several oligopolies emerged during the mid-seventies.[63] Sklair reports that during this time eight oil companies, seven copper companies, six bauxite companies, seven iron ore companies, and a select few tea, coffee, banana and tobacco companies controlled 30%, 25%, 58%, 50%, and 60% of their respective markets.[64]

In the same time period, General Motors' (GM) was carving its own niche in the international economy. Richard J. Barnet and Ronald E. Müller state that in 1973, GM's annual sales were larger than the Gross National Products (GNPs) of Switzerland, Pakistan, and South Africa.[65] According to Charles W. Kegley and Eugene R.Wittkopf, almost a decade later, GM boasted of sales larger than the GNP of almost twice as many countries.[66] By 1992, this corporation's revenues surpassed $133 billion, a figure that exceeded the GNPs of more than nine of the world's countries with five hundred and fifty

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[62] Hamilton, 6-7.

[63] Leslie Sklair, *Sociology of the Global System* (London: Prentice Hall/Harvester Wheatsheaf, 1991), 49.

[64] Ibid.

[65] Barnet and Müller, 15.

[66] Charles W. Kegley, Jr. and Eugene R. Wittkopf, "Nonstate Actors in World Politics," in *World Politics: Trend and Transformation*, Second Edition (New York: St. Martin's Press, Inc., 1985), 153.

million inhabitants.[67] Nineteen ninety-four witnessed 37,000 such corporations control one-third of all private sector assets and attain worldwide sales of $5 trillion.[68]

The Rich Get Richer: The Rise of Income Inequality in the US and the World by Denny Braun claims that the owners of these international corporations subscribe to the notion that all of this wealth can and will be used to alleviate the social situations of the millions of downtrodden citizens of the world.[69] They believe in the free market and the "Midas-like ability" of their companies to bring riches to all of the countries they touch.[70] This belief is a point of contention between proponents and opponents of foreign direct investment. It has fostered one of the most heated debates ever witnessed in the international economic arena. The next two sections outline the positions of both sides.

The Pro-MNC Argument

MNC enthusiasts have their own recollections of economic history. The economic power of Europe during the age of imperialism and the success of the US economy are just a couple of examples that they utilize to attest to the proficiency of foreign investment as a development tool. The injection of foreign capital into these

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[67] Korten, 221.

[68] "The Discreet Charm of the Multicultural Multinational," *Economist* 332, no. 7874 (July 30, 1994): 57-58.

[69] Denny Braun, *The Rich Get Richer: The Rise of Income Inequality in the US and the World* (Chicago: Nelson-Hall Publishers, 1991), 109.

[70] Ibid.

economies has allowed them to enjoy prominent positions in the international economic hierarchy. It has also allowed the citizens of these countries to attain some of the highest per capita GNPs in the world. A present-day demonstration of foreign investment's capabilities is found in Southeast Asia. The economic prowess exhibited by Asia's Tigers (i.e. the countries of Taiwan, Singapore, Hong Kong and South Korea) in the mid-eighties reinforced beliefs in the power of international finance.

Barnet and Müller report that during their colonial conquests European countries became trailblazers in the establishment of international business ventures. The British took pride in the fact that the sun never set on their empire and the French, Dutch, Belgians and Italians tried in earnest to topple the near British monopoly in the sport of "colony grabbing." These conquests not only fed national interests in uncharted territories, but they also aided in the creation the economic powerhouses that still exist today. For example, in its heyday, Great Britain's East India Company, one of the oldest overseas trading organizations, managed to bankroll the largest standing army in the world and provide a steady flow of capital used to replenish the royal treasury and sufficiently fuel the Industrial Revolution.[71]

Katapu argues that foreign investment helped the US in the same manner. The huge investments in heavy engineering industries, which the US received from British and other European sources, considerably aided the country in laying the groundwork for

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[71] Barnet and Müller, 72.

the mechanization and development of its economy.[72] As per Katapu's interpretation, this type of investment allowed the country to acquire the means of production for transport and communications industries, machinery for agriculture, construction and road building, mining and consumer goods producing industries.[73]

Foreign investment also appears to have worked in the same capacity for the countries of Southeast Asia. From meager beginnings, as far as social and economic development are concerned, Asia's Tigers have managed to reap the spoils of capitalist expansion. Take the country of Singapore, for instance. *East Asia's Trade and Investment: Regional and Global Gains from Liberalization*, a World Bank publication, relays the fact that in 1973 Singapore adopted a very generous investment code in order to industrialize its economy.[74] American companies in the petroleum and electronics industries were first in line to take advantage of the liberalization of the Singaporean economy.[75] Eventually, the presence of these companies led to an increase in employment, industrial output, and exports.[76] Additional investments from companies in the manufacturing industry also aided in the growth of the economy. In 1980, manufacturing companies employed 60% of the work force and contributed to 85% of the

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[72] Katapu, 27.

[73] Ibid.

[74] World Bank, *East Asia's Trade and Investment: Regional and Global Gains from Liberalization* (Washington, DC: The World Bank, 1994), 46.

[75] Ibid.

[76] Ibid.

exports.[77] Foreign direct investment from companies in the computer, finance, electronics, machinery, printing, and pharmaceutical industries eventually increased and contributed to two-thirds of the value added.[78] As a result of these huge flows of foreign capital, Singapore is one of the richest countries in the developing world. These accounts of economic history are testaments to the benefits that MNCs can provide prospective host countries (i.e. countries which allow international companies to invest in their economies).

Proponents' View of the MNC

Authors such as K.J. Holsti conceptualize the MNC as a non-territorial, transnational organization characterized by: (1) organized activities occurring simultaneously in a number of countries; (2) objectives that do not relate to interests within any given territory; (3) and component parts that are essentially nonpolitical.[79] According to this description, the MNC is a benign, if not neutral, organization that freely transfers badly needed benefits to the developing economies that host its operations. According to Jan S. Hogendorn, an MNC can provide the following for developing world host economies:[80]

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[77] Ibid.

[78] Ibid.

[79] K. J. Holsti, *International Politics: A Framework for Analysis* (Englewood Cliffs, New Jersey: 1992), 53.

[80] Jan S. Hogendorn, *Economic Development,* Third Edition (New York:

(1) Consumer gain: foreign private investment has the ability to lower the prices of consumer goods by providing a larger quantity and a higher quality of goods formerly produced by inefficient costly producers.

(2) Government revenue: through the taxation of an MNCs inputs, the government can acquire funds for public spending.

(3) Domestic investment: this may be stimulated because MNCs open up opportunities for local firms to supply them with intermediary materials such as components and raw materials.

(4) Production costs: these could be lowered by a coordination of marketing and planning.

(5) Technical knowledge, managerial ability and organizational competence: these can be transferred from foreign to indigenous personnel if an MNC is nationalized.

(6) Income increase through employment opportunities provided by the MNC.

(7) Stimulation of domestic savings rates.

HarperCollins Publishers, Inc., 1996).

All of these benefits are valuable to host countries, but domestic investment appears to be especially important to sustainable development. Domestic investment is also referred to as either a "forward" or "backward" linkage. A forward linkage is created with the host economy when the MNC's finished product is used by other firms in the host economy as an input for their products.[81] A backward linkage results from the intensive use of locally sourced inputs in an MNC's final product. The continued use of domestically produced inputs allows the host country to establish a market for specialized inputs and therefore encourages investment in their production.[82] Hence, domestic investment provides a vehicle through which a host economy's growth and development can become self-generating.

"Multinationals, Linkages and Economic Development" by Andrés Rodríguez-Clare demonstrates that these linkages do materialize in host economies and can positively affect a country's development strategy. His finding is based on the fact that (1) production efficiency is enhanced by the use of a wider variety of specialized inputs, (2) the proximity of supplier and user is essential for many of these inputs, and (3) the size of the market in a host country's limits the availability of a variety of specialized inputs.[83]

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[81] Ibid., 402.

[82] Ibid.

[83] Andrés Rodríguez-Clare, "Multinationals, Linkages and Economic

Theoretical Frameworks of Pro-MNC Argument

The proponents of foreign direct investment have developed many theories to validate this interpretation of the multinational. Most famous amongst these is the theory of foreign direct investment. Katapu's interpretation of the theory is that economic growth and development depend on successfully attracting foreign financial and industrial assets to invest in the industrial base of host countries. Once this is achieved, the host country will acquire the benefits discussed above and experience development.[84]

Theodore Moran and Ted C. Lewellen state that this staunch belief in the power of the MNC is rooted in classical and neo-classical economic theory, namely theories of economic growth.[85] In the fifties and sixties, when economic growth was equated with economic development, theorists such as Walt W. Rostow and Roy Harrod and Evesey Domar received international acclaim for their respective models which emphasized the role of capital and savings in a nation's development. These theories, which can also be referred to as capital flow models, postulated that among the many positive results of foreign capital penetration were an increase in output and an increase in the incomes of host country nationals.[86]

Development," *American Economic Review* 86, no. 4 (September 1996): 853.

[84] Katapu, 21.

[85] Theodore H. Moran, "Multinational Corporations and Developing Countries," in *Multinational Corporations* (Toronto: Lexington Books, 1985), 1; Ted C. Lewellen, "Modernization and Dependency: Theories of Underdevelopment," in *Dependency and Development: An Introduction to the Third World* (London: Bergin & Garvey, 1995), 56.

[86] Rhys Jenkins, "Theoretical Perspectives on the Transnational Corporation," in *Transnational Corporations and Uneven Development* (London: Methuen, 1987), 18.

According to Todaro, it was the success of the Marshall Plan that prompted economists to turn their attentions to the developing world.[87] Curious as to the nature of their development problems, budding developmentalists began to make parallels between the countries of the North (American and European countries) and the countries of the South (countries of Africa, Asia, and Latin America). Rostow, one of the leaders of the modernization school of thought, subscribed to the notion that developed countries had passed through a series of five stages in their development processes. In order to duplicate the success of developed countries, Rostow speculated that developing countries should follow in the exact same footsteps.

Stages of Growth Theory

In *The Stages of Economic Growth: A Non-Communist Manifesto*, Rostow presents the stages of his "Stages of Growth Theory" :[88]

(1) Traditional Society: In this stage of the development process, a country lacks technology and is limited in its capacity to produce. Its economy centers around a highly primitive and inefficient agricultural sector. The prospects of transforming such a society are precluded by decentralized political power.[89]

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[87] Todaro, 73.

[88] W.W. Rostow, "The Five Stages of Economic Growth—A Summary," in *The Stages of Economic Growth: A Non-Communist Manifesto* (Cambridge: Cambridge University Press, 1960), 4-16.

[89] Ibid., 4.

(2) Precondition for Take-Off: Through the development of technology or the transfer of technology from another society, the country enters this stage of development. It is in this stage that the economy develops new methods of producing goods and services, and therefore utilizes its resources more efficiently. Economic growth has begun. Financial institutions begin to appear and investments in transportation, communications and the extraction of raw material for export increases. The coordination of these developments is facilitated by the centralization of political power.[90]

(3) Watershed or Take-Off: In this stage, a nation's economy experiences additional technological development in two sectors—agriculture and industry. Under the direction of a newly emergent political elite, economic growth becomes priority, as evidenced by national policies geared towards promoting it. The rates of investment and savings grow between 5% and 10%. The increased investment produces profits that can be reinvested back into the economy for development.[91]

(4) Drive to Maturity: According to Rostow, this is a period of self-sustaining growth. Investment reaches figures as high as 20% and this allows a country to increase production to exceed the increase in population growth. Technological innovations during this stage aid in the proliferation of new industries and also cause the most inefficient sectors to become obsolete (e.g. agriculture). The country can now

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[90] Ibid., 6.

[91] Ibid., 7.

produce what ever it wants.[92]

(5) The Age of Mass Consumption: This is the final and most prosperous stage. Incomes are raised to the point where the majority of the population demands products not characterized as necessities (i.e. food, water, and shelter). Watches, cars and homes become normative purchases.[93]

Lewellen argues that this theory was very popular among US politicians because it contained important policy implications.[94] According to this book chapter, the US perceived developing countries as potential allies who could possibly aid in the struggle to curb the Communist threat. If their development-related problems could be dealt with, this prospective role could become more of a reality.[95] Government officials thought that if developing countries could reach Rostow's Take-Off stage their economies would become self-sustaining.[96] Lewellen states that the US was willing to provide the transfers of technology and capital to aid in this process.[97]

This theory spurned disagreement between government officials and academics, who did not believe in the universality of Rostow's stages in the developed or developing

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[92] Ibid., 9.

[93] Ibid., 10.

[94] Lewellen, 56.

[95] Ibid.

[96] Ibid.

[97] Ibid.

worlds.[98] Despite the controversy, theories which give equal importance to capital and savings in the growth process did not lose their popularity in development circles. A case in point is the Harrod-Domar model.

Harrod-Domar Model

Gillis, Perkins, Roemer, and Snodgrass have found that in the forties, Roy Harrod and Evesey Domar, who are actually Rostow's predecessors, also created this model with developed countries in mind.[99] This model was initially used to explain the relationship between growth and unemployment in developed economies. As far as developing countries were concerned, the Harrod-Domar model became a way of analyzing the relationship between economic growth and capital requirements.[100]

The major assumption of the model is that the output of any economic unit, be it a firm or an entire economy, depends on the amount of capital invested in it. Where Y stands for a unit's output, K is the stock of capital and k is a constant called the capital output ratio,

$$Y = K/k \tag{2.1}$$

This equation represents the capital-output ratio of the economic unit. In order to

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[98] Ibid.

[99] Malcolm Gillis, Dwight H. Perkins, Michael Roemer, and Donald R. Snodgrass, "Growth and Structural Change," in *Economics of Development,* Third Edition (New York: W.W. Norton & Company, 1992), 43.

[100] Ibid.

indicate a growth in output, the delta sign, or Δ, is inserted into the equation.

(2.2) $$\Delta Y = \Delta K/k$$

Output's growth rate, g, is the change in output, ΔY, divided by the total output, Y and is represented by ΔY/Y. Dividing both sides of equation 2.2 by Y produces the next equation,

(2.3) $$g = \Delta Y/Y = \Delta K/Y \cdot 1/k$$

Gillis, et al. state that for an entire economy, ΔK is the same as investment, which is I. According to this theory, investment must equal savings, S. So, ΔK/Y becomes I/Y and this is equal to S/Y. Furthermore, S/Y can be represented by s, the savings rate, which is also a percentage of the country's national product. The final equation and the basis of the Harrod-Domar model is,

(2.4) $$g = s/k$$

Harrod and Domar subscribed to the notion that investment in plant and equipment determined the amount of growth that a country experienced. Savings by citizens and corporations make this investment possible.

Hogendorn claims that this theory was considered a revolution in development economics in developing countries. By using the incremental capital-output ratio (ICOR), which differs from the capital-output ratio in that it measures the effect of additional or incremental capital on growth, economists in developing countries could actually determine the amount of savings and investment necessary to achieve desired growth rates. Todaro provides an excellent example of this practice. If a country desires an output growth rate, g, of 7% and its ICOR is 3, the country needs an annual savings rate of 21%.[101] Say the amount of domestic savings is 16%, then the country is said to have a savings gap of 5%. The ability of a country to fill this gap with foreign capital from foreign direct investment or aid will determine whether or not it reaches its expected rate of growth.

One might think that these theories validated the existence of MNCs in developing countries and concretely established a permanent place for them in international circles. According to Sayre P. Schatz, Raymond Vernon extols the virtues of the tripartite relationship between international trade, foreign capital penetration and the positive effects on growth and development. He proposes that MNCs promote specialization on a world scale, which increases the gross world product and provides a higher quality of life for the world's inhabitants.[102] Specialization promotes efficiency in world production, which in turn heightens interest in research and development activities and the funding of productive investments that, in the absence of the MNC, would otherwise go unattended.[103] All of these factors should result in the attainment of the

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[101] Ibid.

[102] Sayre P. Schatz, "Assertive Pragmatism and the Multinational Enterprise," in *Postimperialism: International Capitalism and Development in the Late Twentieth Century* (London: Lynne Rienner Publishers, 1987), 108.

[103] Ibid.

various benefits listed above.

Theodore Moran, Michael Todaro, and Rhys Jenkins have all found that the tenets of classical and neo-classical theory depend heavily on the realization of various assumptions surrounding market behavior.[104] Most critical among these assumptions are what Jenkins refers to as the supplement assumption, the competitive assumption and the resource generation assumption.[105]

The supplement assumption states that foreign resources supplement domestic resources. In other words, an MNC provides a country with the foreign exchange, export revenue, locally raised taxes, managerial know-how and technology that would be otherwise unavailable in its absence. Furthermore, without these resources there would be no local production. According to the competitive assumption, the market exists in an environment of perfect competition wherein economic factors (i.e. countries or business enterprises) adhere to the principle of comparative advantage and refrain from interfering in the free workings of the market.[106] Lastly, the resource generation assumption claims that, in addition to supplementing local resources, MNCs produce more local resources or use previously idle resources.[107]

Collectively, these assumptions underlie the belief that MNCs aid in the efficient

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[104] Ibid., 3; Todaro, 531-533; Jenkins, 19.

[105] Jenkins, 19.

[106] Ibid.; Todaro, 425.

[107] Jenkins, 19.

allocation of resources on an international scale for the betterment of humankind. In his chapter entitled, "How a Multinational Corporation Appears to Its Managers," Jacques G. Maisonrouge, chairman and chief executive officer of the IBM World Trade Europe/Middle East/Africa Corporation in the seventies, even goes as far as to dub MNCs, the "great equalizers among nations" and the "catalysts of progress."[108] He argues that the international company is the best tool, yet to be devised, that can solve problems of inflation, skyrocketing oil prices, poor harvests and rising unemployment.[109] Maisonrouge justifies this statement by pointing to the fact that a purely political solution to these problems has yet to surface.[110] However, several of humankind's instincts—self-interest, competitiveness, and the need to be part of something bigger—can all be harnessed under the auspices of corporate organization for the greater good.

Business International Corporation, a service organization for international corporations, expresses these same sentiments. Barnet and Müller quote the organization claiming that,

> International corporations possess a high proportion of the technology, the managerial talent and private capital required for the solution of the economic and social problems of this planet. They can tackle development of the

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[108] Jacques G. Maisonrouge, "How A Multinational Corporation Appears to Its Managers," in *Global Companies: The Political Economy of World Business,* ed. George W. Ball (Englewood Cliffs, New Jersey: Prentice-Hall Inc., 1975), 15.

[109] Ibid., 11-12.

[110] Ibid., 13.

> resources of the sea, economic development of poor countries, new housing everywhere, the protection of the human environment, the training of people for skilled managerial and technical work, and the creation of jobs for underprivileged people.[111]

The prospective benefits of foreign investment are indeed impressive. If these countries could manage to actually obtain the technology, capital and employment opportunities, and disburse them equitably throughout all sectors of their economies, foreign investment could be properly regarded as a development tool. Unfortunately, as far as developing countries are concerned, the pro-MNC argument is not based on a realistic assessment of the international economic system, but on a belief system Korten refers to as the "Illusion of the Cloud-Minders."[112]

Cloud-Minders are those who exist in the upper echelons of global society. They are the owners and managers of corporations and the bourgeoisie from developed and developing societies. Their lives do indeed take place above the clouds (i.e. high rises, private jets and controlled access communities)—lives of privilege. Even though members of these classes are bonded to each other through similar beliefs and ideologies, such as the magic of the market to bring about social change, they are quite detached from larger segments of society. They are oblivious to the reality that their very existence continuously drains the world of resources.

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[111] Barnet and Müller, 62.

[112] Korten, 104.

Korten states that this naiveté is reinforced by organizations such as the World Bank and the IMF, which he describes as, "leading proponents of economic rationalism and free-market, export-led growth strategies."[113] These organizations are famous for applauding the success stories of the developing world: Ghana, Ivory Coast and Asia's Tigers. The illusion is also bolstered by glorification of wealth and the wealthy by the business press and the studies of economic researchers and consultants.[114] However, this illusion falters when one takes into account the negative effects of MNCs on the economies of lesser-developed host countries.

The Con-MNC Argument

To the average observer, MNCs appear to uphold the principles of *laissez-faire* and behave in a manner becoming business enterprises. They even seem to go above and beyond the call of duty. MNCs have been known to assist in community economic development, engage in minority employment practices, and other various types of social affairs programs.[115] David Korten states that these are some of the strategies that MNCs use to present themselves as "good local citizens."[116] However, this identity is fleeting in nature: cultural identities are quickly shed when they interfere with the corporation's

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[113] Ibid., 105.

[114] Ibid.

[115] Barnet and Müller, 359.

[116] Korten, 125.

political or economic interests.

The research findings in *Global Reach: The Power of the Multinational Corporations* by Richard J. Barnet and Ronald E. Müller confirm these accusations. According to these authors, the benefits discussed in the previous section almost never accrue to developing countries. Since the primary concern of these corporations is to organize and integrate economic activity around the world in such a way as to maximize global profit, MNCs have been less concerned with providing these benefits and more concerned with subverting the sovereignty of their respective host nations.[117] Political corruption, failure to transfer technology, control of a country's money supply, and exclusionary employment practices are just a few of the ways that multinationals maintain a dependent relationship between themselves and developing host countries and ensure goals of capital accumulation.

Political Corruption

In *Contending Theories of International Relations: A Comprehensive Survey,* James Dougherty and Robert Pfaltzgraff, Jr. report that these organizations have gone on record as having readily interfered in a host country's political and economic life, so as to create a stable environment for their investments.[118] They state that MNCs have been

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[117] Barnet and Müller, 373.

[118] James E. Dougherty and Robert L.Pfaltzgraff, Jr., "Theories of Imperialism and Economic Causes of International Conflict," in *Contending Theories of International Relations: A Comprehensive Survey,* Third Edition (New York: HarperCollins Publishers, 1990), 254.

found guilty of serving foreign policy interests of their respective governments, engaging in intelligence gathering acts, and pressuring their parent states to pass laws and pursue diplomatic policies that would promote their interests.[119]

In addition to its accounts of MNC activity in Africa, Louis Turner's work, *Multinationals in the Third World,* expounds on their activities in other developing countries. In 1910, a United Fruit (now United Brands) company official staged an invasion of the country of Honduras in order to preclude American businessman, J. Pierpont Morgan, from acquiring a stake in the country's banana industry.[120] The company hired a mercenary by the name of Machine Gun Maloney with the goal of attaining monopoly status in the Honduran banana industry. In 1954, the same company collaborated with the Central Intelligence Agency (CIA) of the United States to initiate a coup to oust then president, Jacobo Arbenz Guzmán, in retaliation for his land reform program.[121]

In another region of the globe, Barnet and Müller claim that the American company, International Telephone and Telegraph (ITT), played both sides of the fence during World War II.[122] Company executives are said to have gathered intelligence from

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[119] Ibid., 254-255.

[120] Turner, 22.

[121] Ibid., 23.

[122] Barnet and Müller, 60.

Hungary and Germany for the American government.[123] The company's ties with the German government prior to the war also allowed them to provide communication services to Nazi forces throughout the entire war.[124] The company created a very comfortable position for itself. Regardless of the outcome, it would have come out on top.

Kegley and Wittkopf present the fact that this same company used its connections with the US government again in Chile around 1970.[125] In order to protect its interests in the Chiltelco telephone company, ITT devised a plan to prevent the Marxist candidate, Salvador Allende from being elected. As was the case with UMHK in Zaire, ITT financially supported Allende's opponent.[126] After Allende won, the company prompted the American government to adopt policies that would disrupt the Chilean economy.[127]

Multinationals have gone far beyond military intimidation and intelligence work to create suitable trade environments. Nineteen seventy appears to have been a popular year for multinational activities. Kegley and Wittkopf state that in the same year MNCs lobbied the US government to pass legislation that warranted the removal of foreign aid

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[123] Ibid.

[124] Ibid., 61.

[125] Kegley and Wittkopf, 156.

[126] Ibid.

[127] Ibid.

from countries that nationalized US investments overseas without just compensation.[128] These authors have also found that MNCs used their lobbying powers to bring about the creation of the liberal multilateral trade system and the trade and taxation policies that support it.[129]

Samuel M. Muriithi's findings in *African Development Dilemma: The Big Debate* are consistent with those of Barnet and Müller and Turner. He demonstrates how MNCs use local governments to further their interests. MNCs bribe government officials and launch pricey campaigns in order to discourage the development of local industry and guarantee a market for their products.[130] According to Muriithi, MNCs temporarily lower the prices of their products to muscle local industries out of the market.[131] This practice, formally referred to as dumping, works to render the domestic production of similar products obsolete.

Accounts of political corruption by MNCs are unfortunately quite numerous. To discuss all of them is beyond the scope of this research. However, MNC behavior in terms of technology transfer equally contributes to the negative perception of MNCs.

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[128] Ibid., 157.

[129] Ibid.

[130] Samuel M. Muriithi, *African Development Dilemma: The Big Debate* (Lanham, Maryland: The University Press of America, 1997), 90.

[131] Ibid.

Technology

MNCs do not share with or transfer their technology to their respective host countries. Barnet and Müller claim that MNCs withhold technology from developing nations by not transferring it to indigenous managers.[132] When technology is shared, it is often inappropriate for the local industry's production needs.[133] In other words, capital intensive technology, such as a tractor or bulldozer is offered to host economies with scarce capital resources.[134] Despite this fact, many developing country officials, who view technology as badges of progress, purchase such items. This seriously drains host countries of capital that could be used in another capacity. Lastly, attempts of developing countries to create technology of their own are thwarted by the fact that companies in developed countries own a majority of the patents.[135] Barnet and Müller cite a 1964 United Nations study which demonstrates this fact. In India, Turkey, the United Arab Republic, Pakistan and Trinidad, eighty-nine percent of all patents were foreign-owned.[136] A later study shows that the percentage of foreign-owned patents jumped from 65% in 1937 to 95% in 1965.[137] *Earth Island Journal* reveals that today, multinationals

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[132] Barnet and Müller, 140.

[133] Lewellen, 114.

[134] Barnet and Müller, 168.

[135] Ibid., 140.

[136] Ibid.

[137] Ibid.

as a whole control 90% of all technology and product patents.[138]

Hence, with the relocation of a firm to another country or region, most countries are no better off than when the company arrived. B.N. Ghosh refers to this aspect of MNC behavior as "technological neocolonialism" due to the fact that their main objective is to ultimately maintain developing countries dependence on them for technological know-how.[139] Irfan ul Haque discusses the implications of this brand of neocolonialism. He argues that a country's lack of technological know-how prevents the development of new products and production processes, economic expansion and, in the long run, human and economic development.[140] Similar effects are achieved by MNCs control of capital in host countries.

Control of Capital

Robert Carbaugh's *International Economics*, Barnet and Cavanagh, Barnet and Müller, and Braun all agree that MNCs seize control over the money supply in developing countries. First of all, they have been known to engage in the infamous practice of transfer pricing. In order to avoid high tariffs in developing countries, an MNC reports most of its profits in low-tax countries, when in reality it has earned them in

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[138] "Controlling the Transnational Outlaws," *Earth Island Journal* 12, no. 4 (Fall 1997): 39.

[139] B.N. Ghosh, "Fundamentals of Neocolonialism," in *Political Economy of Neocolonialism in Third World Countries* (New Dehli, India: Sterling Publishers Ltd., 1985), 15.

[140] Irfan ul Haque, "Technology and Competitiveness," in *Trade, Technology and*

high tax countries.[141] In other words, corporations ensure that their profits are reported in regions where tax structures are more lenient or do not exist at all.[142] Bearing in mind that most developing countries obtain a significant amount of public revenue from indirect taxes like these, it is apparent how this action also robs host countries of capital that could potentially be used for social reform purposes.[143]

Braun cites a study which explains how companies get away with this practice. According to Bornschier and Chase-Dunn, half of world trade occurs between and amongst MNCs.[144] Oftentimes, MNCs form oligopolies or conglomerates which allow them to trade with themselves and determine the prices of their imports and exports, which in turn allow them to maximize profit.[145] The free market is completely avoided. It is quite rare for MNCs to have to answer to governments or international organizations established to monitor their activities.[146]

The MNC's power over the money supply is also evidenced by the fact that local

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International Competitiveness (Washington, D.C.: The World Bank, 1995), 11.

[141] Robert J. Carbaugh, *International Economics,* Fifth Edition (Cincinnati, Ohio: South-Western College Publishing Co., 1995), 292.

[142] Barnet and Cavanagh, 345.

[143] E. Wayne Nafziger, *The Economics of Developing Countries*, Third Edition (Upper Saddle River, New Jersey: Prentice Hall, 1997), 403.

[144] Braun, 115.

[145] Lewellen, 111.

[146] Braun, 115.

banks will lend them money more readily than local entrepreneurs.[147] Some of these banks even offer MNCs loans with extremely low or negative interest rates.[148] The reason for this behavior is that domestic banks perceive MNCs as more creditworthy than domestic producers.[149] In the short-run, favoring MNCs over indigenous producers appears to be a prudent business move. However, in the long run this perception precludes the development of infant industries because very little capital is left after MNCs take the lion's share.[150]

Transfer pricing and exclusionary loan practices obviate the need for MNCs to engage in domestic investment in the host country. In "Multinationals, Linkages and Economic Development," Andrés Rodríguez-Clare acknowledges the existence of backward and forward linkages in host economies.[151] However, his study reveals that the development of these linkages is more likely to occur in more developed host countries.[152] This is due, in part, to the fact that a variety of intermediate inputs are becoming increasingly available in developed countries, where most multinationals are

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[147] Barnet and Müller, 141; Lewellen, 113.

[148] Barnet and Müller, 141.

[149] Lewellen, 113.

[150] Ibid.

[151] Rodríguez-Clare, 853.

[152] Ibid., 867.

based.[153]

A United Nations study implies that lack of domestic investment disrupts a developing host country's balance-of-payments.[154] The capital generated from trade through MNCs is never really enjoyed because of the excessive borrowing host country's required to offer MNCs the loans which were used to attract them to the country in the first place.

The result of these practices is a significant degree of capital flight from developing countries. Ghosh reports that MNCs have been known to take anywhere between $50-$100 billion from developing countries annually.[155]

Employment

"Transnational Corporations" by Ghosh highlights the issue of job creation.[156] A positive aspect of this issue is that MNCs offer higher wages than local firms. A problem arises, however, because this increases the demand for higher wages in other industries. This situation is referred to as wage inflation.[157]

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[153] Ibid., 868.

[154] Braun, 112.

[155] B.N. Ghosh, "Transnational Corporations," in *Political Economy of Neocolonialism in Third World Countries* (New Dehli: Sterling Publishers Priv. Ltd., 1985), 68.

[156] Ghosh, 72.

[157] Ibid.

According to Todaro, wage inflation increases unemployment rates in host countries.[158] The traditional competitive free-market model states that employment and wage rates are determined by the prices in the economy and factor uses in the production process, which are, in turn, determined by supply and demand.[159] Producers are more apt to demand additional workers so long as the value of the workers' marginal product is greater than the wage provided. Unfortunately, this is not the case in many developing countries.[160] Wage inflation increases the cost of labor to the point where it is unprofitable for producers to hire more workers. The wage inflation phenomenon, therefore, lends itself to an increase in unemployment. The majority of an able-bodied workforce is left unemployed because it is simply too expensive to hire them.

Even though MNCs offer higher wages, domestic workers are still under-compensated in comparison to foreign nationals. Ghosh reports that the salaries which indigenous professionals receive from MNCs are almost eight to ten times lower than those in developed countries.[161] At the same time, some host-governments compensate foreign nationals anywhere from seven to fourteen times more than indigenous, equally experienced workers.[162]

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[158] Todaro, 234.

[159] Ibid., 233.

[160] Ibid., 234.

[161] Ghosh, 72.

[162] Ibid.

This employment structure not only supports huge income disparities, but it also leads to frustration and ultimately the proliferation of the brain drain phenomenon.[163] Many developing regions, especially sub-Saharan Africa, have suffered the loss of high quality manpower (HQM) or skilled professionals, to developed countries where their services are better compensated.[164] Ghosh says that the loss is permanent in that it significantly reduces productivity, obstructs the growth of intellectual leadership and impedes the country's innovative spirit.[165]

MNCs unwittingly suffer at the hands of their own hiring practices. "Global Staffing: Are Expatriates the Answer?" by Kenneth Groh and Mark Allen ascertains that a majority of international companies prefer to employ expatriates over indigenous managers.[166] Groh and Allen state that these companies are shortchanging their overseas operations. The authors cite a study of forty companies, which found that those organizations with a higher number of "globally mobile" employees had lower rates of returns to shareholders.[167] Companies with higher rates of returns employed 50% fewer expatriates and used regional transfers and third-country nationals more frequently.[168]

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[163] Ghosh, 20.

[164] Ibid., 111.

[165] Ibid., 112.

[166] Kenneth Groh and Mark Allen, "Global Staffing: Are Expatriates the Only Answer?" *HR Focus* 75, no. 3 (March 1998): S1.

[167] Ibid.

[168] Ibid.

From the discussion so far it is apparent that the notion of job creation is basically inadmissible as a prospective benefit of MNC occupation. Luigi Brunamonti's findings support this claim. In "Multinational Corporations and the Civil Society," Brunamonti indicates that 500 of the world's major corporations only employ 0.05% of the world's population.[169] One reason for this situation concerns the use of inappropriate technology in MNC production.

In the sub-section concerning technology, it was noted that, more often than not, capital-intensive technology is introduced into labor-intensive developing host economies. Since the technology available to the developing world is becoming more and more advanced, additional capital is needed to hire individual workers.[170] At the same time, capital introduced by multinationals is subsidized by interest rates offered to them by host countries, and the host countries' inability to control transfer pricing.[171] Economist James Grant refers to this trend as the "artificial cheapening of the price of capital and the artificial increase in the price of labor."[172] Technological innovation contributes to unemployment problems in labor-intensive economies.

Leslie Sklair and Agbeko Katapu agree that the jobs that MNCs do bring to the host country come with a cost. Katapu states that foreign investors interested in making

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[169] Luigi Brunamonti, "Multinational Corporations and the Civil Society," *International Journal on World Peace* 14, no. 2 (June 1997): 109.

[170] Barnet and Müller, 169.

[171] Ibid., 170.

[172] Ibid.

quick returns concentrate on industries which do not typically contribute to the economic growth and development agendas of host countries.[173] Most popular among these are the export processing zones, or EPZs. Praised for their positive effects on growth and development in countries such as Singapore, Mauritius and Mexico, EPZs offer low wage employment which is monotonous and sometimes physically taxing.[174] Offered almost exclusively to women, jobs in EPZs contribute to the change in the sexual division of labor in host societies.[175]

Sklair cites various studies which claim to pinpoint the reason why women are employed more often in these industries. For some companies, it is simple economics. A study by Hein reveals that in Mauritius it is a government mandate that women receive a lower minimum wage than men.[176] Others say that women are targeted because they are assumed to be more docile, especially when it comes to the formation of unions.[177]

Whatever the reason, Sklair states that these employment trends are contributing to a male-dominated state sector and an industrial labor force which is constantly being increased by more women in private foreign owned industry.[178] They are also said to be disrupting traditional family life.[179]

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[173] Katapu, 27.

[174] Sklair, 65.

[175] Ibid., 110.

[176] Ibid., 111.

[177] Ibid., 112.

"Multinational Corporations in the Making and Unmaking of Ethnic Groups" by Cynthia H. Enloe declares that the hiring practices of MNCs create and dissipate ethnic cleavages in indigenous populations to meet profit-maximizing needs.[180] Enloe observes the fact that earlier international corporations and the MNCs of today used similar hiring techniques that have had adverse effects on ethnic relations.[181] Both obtained labor from outside the host country if they found that indigenous populations were "unsuitable" for the type of work they required.[182] Enloe outlines three effects of this practice:[183]

- The introduction of a growing number of the world's poor into a direct relationship of dependency in international economic system;
- The perpetuation and exacerbation of gaps between territorially defined groups or between rich and poor;

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[178] Ibid., 110.

[179] Ibid., 113.

[180] Cynthia H. Enloe, "Multinational Corporations in the Making and Unmaking of Ethnic Groups," in *Ethnonationalism, MNCs and the Modern State*, vol. 15, book 4 of the Monograph Series in World Affairs, eds. Ronald M. Grant and E. Spencer Wellhofer (Colorado: University of Denver Publications, 1979), 9.

[181] Ibid., 10.

[182] Ibid.

[183] Ibid., 11.

- The accentuation of ethnic divisions in countries where firms established operations.

Enloe states that these practices are responsible for the political tensions in Java and Guyana, social stratification in Namibia, and workers strikes in England.[184]

Despite these realities, governments in developing countries still strive to attract foreign investment to their economies. One of their strategies is to temporize on the issue of union activities that could undermine the union's call for competitive wages, benefits, and adequate labor standards.[185] Governments are also famous for implementing generous investment codes or policies.

Investment Codes

Since the potential benefits of MNC presence are so enticing and there are so many countries vying for a company's attention, the competition is fierce. Incentives offered frequently subvert the development efforts of host countries. For example, Gillis et al. state that MNCs are provided with tax holidays.[186] These are periods of time during which companies are exempt from paying taxes to their host countries. Tax holidays last

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184 Ibid., 14, 17.

185 Korten, 165.

186 Gillis et al, 318.

anywhere between 3 and 10 years or more.[187] Host governments also give MNCs tax credits which make it possible for them to withhold a portion of their taxable income.[188] Sometimes, MNCs are allowed to withhold 20%-25% of their income.[189] Furthermore, MNCs are given subsidies that local businesses would be privileged to receive.[190] They receive help to construct plants and train employees.[191] Lastly, MNCs are enticed by loan guarantees, investment insurance and guarantees for full or partial repatriation of their profits.[192]

In addition to these incentives, host countries are obliged to provide a favorable investment climate to companies pondering the prospect of investing in their countries. According to Lewellen, a favorable investment climate includes:[193]

- A stable economy and government.
- Adequate infrastructure, such as roads, communication systems, etc.
- Sufficient domestic savings.

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[187] Ibid..

[188] Ibid.

[189] Ibid.

[190] William A. Stoever, "The Stages of Developing Country Toward Foreign Investment," *Columbia Journal of World Business* 20, no. 3 (Fall 1985): 4.

[191] Ibid.

[192] Ibid.

[193] Lewellen, 112.

- Regulations, licensing requirements, laws, etc. to achieve investment objectives.

These provisions, in addition to the tax holidays and subsidies, put a large amount of pressure on the economies of host countries, which are desperate for capital in the first place. To reiterate, these offers marginalize the needs of the poor in that less money is spent on social needs, such as education and health care.

However, developing countries press on in their quest to attract foreign investment. One of the most controversial attempts to do so was the establishment of the Economic Development Act (EDA) by President France Albert Rene of the Republic of the Seychelles in November 1995.[194] "Investment à la Seychelloise" by the *Economist* reports that this investor-friendly legislation provided various tax privileges and certain protections to investors (criminal or legitimate) who were willing to invest a minimum of $10 million in the Seychellois economy, no questions asked.[195] Robert E. Barnett states that some of the incentives offered were immunity from prosecution and safeguards against the seizure of an investor's assets.[196] International organizations such as Interpol, British Serious Fraud Office, the European Union and committees of the Organization of the Economic Cooperation and Development (OECD) were opposed to the EDA due to its implications for money laundering in the international system.[197] President Rene

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[194]"Seychelles Caught in the Act," *Banker* 146, no. 846 (August 1996): 9.

[195]"Investment à la Seychelloise," *Economist* 338, no. 7953 (February 17, 1996): 39.

[196] Robert E. Barnett, "FATF Questions Seychelles Foreign Investment Law," *Financial Regulation Report* (March 1996): 8.

denied furthering money-laundering agendas and remained steadfast in his commitment to the legislation until 1996. Under pressure from anti-money laundering groups such as the Financial Action Task Force (FATF), the act was revoked and replaced by the Anti-Money Laundering Act.[198]

Legislation like the EDA will continue to surface as long as host countries remain dependent on MNCs for the aforementioned benefits. And, Robert B. Siedman claims that, "as long as private capital enters a country unhindered, it commands the local economy."[199]

The Transfer of Ideology

Another factor that prompts host countries to actively pursue MNCs is the effect that these corporations have had on the mentalities of host country nationals. Sklair argues that a certain type of value system is required for the successful transformation into a modern capitalist society: the culture ideology of consumerism.[200] Barnet and Müller state that MNCs have aided in this transformation by obtaining control of communication venues that influence the tastes, goals and values of workers, suppliers, government officials and consumers.[201] Corporations continuously peddle the ideology

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[197] Ibid.

[198] "Seychelles Caught in the Act": 10.

[199] Robert B. Siedman, "Foreign Private Investors and the Host Country," *Journal of World Trade Law* 19, no. 6 (November/December, 1985): 645.

[200] Sklair, 147.

that the wealth and prosperity of Western countries can be experienced through the purchase of products produced by foreign companies. Lewellen agrees with Barnet and Müller. He states that in countries with extremely high rates of malnutrition, processed foods with no nutritional value are practically forced onto consumers through pricey advertising campaigns.[202] Companies which sell baby formula are guilty of using these tactics on unsuspecting mothers in the developing world.[203]

The end result of relentless advertising campaigns is the devaluation of locally produced goods in favor of these mass produced products. Muriithi argues that lesser-developed host countries are inevitably transformed into consumer societies: their cultures and economies forever distorted by whims of the monopolies and oligopolies that have taken over.[204] Local production is rendered obsolete in the MNC's pursuit of global expansion.

The influence wielded by MNCs in developing host countries makes it difficult to monitor and curb their activities. The next sub-section will expound on what is being done in this respect.

Legal Venues

According to Kegly and Wittkopf, the regulation of MNCs is a challenging

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[201] Barnet and Müller., 143.

[202] Lewellen, 114.

[203] E. Wayne Nafziger, *The Economics of Developing Countries,* Third Edition (Upper Saddle, New Jersey, Prentice Hall, 1997), 453.

undertaking because of their complex patterns of ownership and licensing agreements.[205] These factors make it difficult to equate an MNC's interests with specific national jurisdictions.[206] As international organizations such as the United Nations (UN) and the World Trade Organization (WTO), whose operations were formerly handled by the General Agreement on Trade and Tariffs (GATT), have increasingly come to realize the implications of multinational activity on developing countries, various mechanisms have been implemented to improve the lot of developing countries in the international system.

The WTO, established in 1995, officially deals with the ill-famed dumping practice. It provides specific guidelines as to how a government can or cannot react to this practice. *Trading into the Future,* a document found on the WTO's web site, states that in order to fulfill the terms of its Anti-Dumping Agreement host governments must, (1) show that dumping is taking place through intense investigation (2) calculate the extent of the dumping (how much lower the MNCs price is than domestic prices), and (3) demonstrate that dumping is causing injury to the economy.[207] Once all of these prerequisites are met, a government is then at liberty to impose taxes on the company's exports and imports, so that the prices of their products are more competitive with domestic prices.[208]

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[204] Muriithi, 91.

[205] Kegley and Wittkopf, 158.

[206] Ibid.

[207] Available from http://www.wto.org/wto/download/download.htm; Internet; accessed June 12, 1998.

The United Nations Commission on Trade and Development (UNCTAD) web site reveals that one of its main objectives is to increase the trade, investment, and development opportunities of lesser-developed countries (LDCs).[209] In pursuit of this objective and in an attempt to prevent further exploitation by MNCs, UNCTAD officials engage in extensive research, policy analysis and intergovernmental deliberations. These activities are geared toward the development of micro-, small-, and medium sized enterprises.[210] Louis T. Wells, Jr. has found that smaller multinationals are more prone to utilize labor-intensive technology, which increases employment and contributes to economic development.[211] UNCTAD officials also help developing countries to promote inward investment and refine their investment climates.[212]

One might think that these improvements in the international system are changing the perception of those opposed to foreign investment. However, this is not the case. As evidenced by the theoretical framework in the next section, much more needs to be done to undo the damage that developing countries have suffered at the hands of MNCs.

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[208] Ibid.

[209] Available from http://www.unctad.org/en/aboutorg/aboutorg.htm; Internet; accessed April 10, 1998.

[210] Ibid.

[211] Louis T. Wells, Jr. "Small-Scale Manufacturing as a Competitive Advantage," in *Multinational Corporations: The Political Economy of Foreign Direct Investment,* ed. Theodore H. Moran (Toronto: Lexington Books, 1985), 119.

[212] Available from http://www.unctad.org/en/aboutorg/aboutorg.htm; Internet; accessed April 10, 1998.

Theoretical Frameworks of Con-MNC Argument

Many opposed to presence of multinationals in the developing world are staunch supporters of the dependency theory. Even though it was developed in the Latin American context, the theory is readily transferable to the problems related to MNC-activities and under-development in sub-Saharan Africa.

"Understanding Latin American Politics" by Gary W. Wynia states that the problems of Latin American development can be traced back to colonial days.[213] Countries in the region essentially began their journey toward economic development as satellites of Spanish and Portuguese economies. Every economic decision, particularly the terms of trade which colonies received for the products that they produced, was made by the mother countries.[214] Since these colonial powers neglected to foster the development of industries outside of agriculture, Latin American countries remained primary-product (natural resource), export economies which were heavily dependent on foreign investment and consumer markets from Spain and Portugal well after independence.

Magnus Blomström and Böjorn Hettne indicate that sub-Saharan African countries have faced and continue to experience the same situation.[215] Despite years of

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213 Gary W. Wynia, "Understanding Latin American Politics," in *The Politics of Latin American Development* (Cambridge: Cambridge University Press, 1984), 126.

214 Ibid.

215 Magnus Blomström and Böjrn Hettne, "The Scramble for African Capitalism," in *Development Theory in Transition, The Dependency Debate and Beyond: Third World Responses* (London: Zed Books, 1985), 142.

freedom from colonial rule and exposure to the international system, most of the countries in this region still obtain the majority of their foreign exchange from the export of primary-products whose prices are determined by American and European countries. Blomström and Hettne present Samir Amin's explanation of the situation facing developing countries as a whole. Amin postulates that the global capitalist system consists of two types of capitalism.[216] The first type exists in developed countries (center) and is referred to as autocentric, dynamic capitalism. The second type, which exists in developing countries (periphery) is referred to as blocked capitalism. Amin states that these types of capitalism are linked and the system reproduces itself on a global level. Figure 2.1 illustrates the relationship between the two.

According to Amin, the key to sustainable capitalism is a link between the production of consumption goods and production of capital goods.[217] Blomström and Hettne use Marx's analysis of capitalism to demonstrate this link. Marx's writings postulate that in 'pure' capitalist societies wages are defined differently from the perspective of the producer and the consumer.[218] As far as the producer is concerned, higher wages translate into higher production costs. However, workers need higher wages in order to purchase the goods that the producer provides. 'Normal' capitalist growth puts a lower limit on wages, but not to the extent where it significantly impedes

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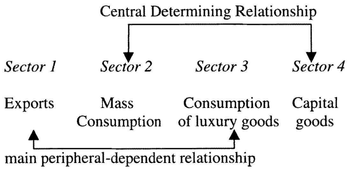
[216] Ibid.

[217] Ibid.

[218] Ibid.

Figure 2.1
Samin Amir's Model of Central and Peripheral Capitalism



Source: *Development Theory in Transition: The Dependency Debate & Beyond: Third World Responses,* (London: Zed Books, Ltd., 1985), 143.

mass consumption. This is the type of capitalism that exists in the center. It is autocentric and dynamic in that it is self-perpetuating: with the wages that producers offer and the resultant purchasing power of the consumer, capitalism in the center continues to develop on its own.

The link between production of consumer and capital goods does not exist in the periphery. The pre-capitalist mode of production that existed in this sector enabled producers to lower wages because it was assumed that workers obtained part of their livelihood from the traditional or pre-capitalist sector.[219] Amin states that this action isolated the agricultural sector from the rest of the economy.[220] The export structure was geared toward the production of primary products, but the market for these products did not exist in peripheral countries. It was in the center. Meanwhile, 'parasitic' social groups, such as the bourgeoisie, created demands for luxury goods in the periphery.[221] These demands could only be satisfied by production in the center. Therefore, the production of primary products is not sustained because there is no market for them.

E. Wayne Nafziger cites a Brazilian economist by the name of Celso Furtado to explain the effects of this situation. The natural resources taken from the export structures in the periphery are channeled into the manufacturing industry of center.[222] The result is

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[219] Ibid.

[220] Ibid., 144.

[221] Ibid.

[222] E. Wayne Nafziger, *The Economics of Developing Countries*, Second Edition (Englewood Cliffs, California: Prentice Hall, 1990), 91-92.

an increase in productivity in the center accompanied by new consumption patterns in the periphery. In effect, a "peripheral capitalism" is created.[223] This brand of capitalism is unable to generate innovations and is dependent for transformation on decisions made from the outside. In essence, the periphery is left drained, "dependent" on the center for survival. Andre Gunder Frank refers to the situation as the "development of underdevelopment."[224]

As far as this theory is concerned, MNCs behave as the primary agents of resource extraction. By establishing subsidiaries in several developing countries, they contribute to the international division of labor by denying, their host countries the previously mentioned benefits. Many host countries are left bereft of the spoils of capitalism—dependent on international corporations for survival.

"Why Postimperialism?" in *Postimperialism: International Capitalism and Development in the Late Twentieth Century* introduces the role of the developing host country's bourgeoisie or political elite in the perpetuation of dependence in developing countries.[225] As the primary consumers of luxury goods, they provide a steady market for products from developed countries. Also, as leaders of government and champions of private enterprise, the bourgeoisie develop strong ties with the owners and managers of

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[223] Ibid., 92.

[224] Phillip King, "The Multinational Corporation: Pro and Con," in *International Economics and International Economic Policy: A Reader* (New York: McGraw-Hill Publishing Company, 1990), 235.

[225] Becker and Sklar, 6-7.

international corporations. Corporations look to the local bourgeoisie to provide stable, political environments in which they can thrive and the local bourgeoisie procure jobs and/or bribes for their cooperation. This affiliation has led to the creation of what David G. Becker and Richard L. Sklair refer to as the "managerial bourgeoisie" or what Leslie Sklair term as the "transnational capitalist class" (TCC).[226] Devoid of geographical or cultural ties, the members of this class are bound together by the belief in the market to bring about significant social change.

It appears very unlikely that a détente can be reached between those who vehemently defend and attack the MNC phenomenon. However, Sayre P. Schatz proclaims that there is a middle ground of sorts.

Assertive Pragmatism

In "Assertive Pragmatism and the Multinational Enterprise," Schatz claims that the social sciences are plagued by a degree of uncertainty which does not lend itself to a realistic assessment of issues such as the supposed benefits or costs of the presence of an MNC in a developing country.[227] This uncertainty principle, therefore, renders the positions of those who subscribe to and oppose the MNC phenomenon as counter-factual

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[226] Ibid., 9; Sklair, 70.

[227] Sayre P. Schatz, "Assertive Pragmatism and the Multinational Enterprise," in *Postimperialism: International Capitalism and Development in the Late Twentieth Century*, eds. David G. Becker, Jeff Frieden, Sayre P. Schatz, and Richard Sklar (London: Lynne Rienner Publishers, 1987), 112.

and highly speculative.[228] Assertive pragmatists, on the other hand, realistically define the dilemmas facing developing countries in an economic system that is increasingly being overrun by MNCs. Aware of the power and influence of MNCs, assertive pragmatists ask the question, "in the existing real-world situation, by what means can welfare be enhanced?"[229]

This mode of reasoning prompts pragmatists to bargain with multinationals in situations where proponents or opponents would reach stalemates.[230] Even though bargaining with MNCs involves a great deal of risk, pragmatists should not be perceived as risk takers. They reject offers which promise short-term benefits because of potential negative effects in the long run.[231] However, they embrace piecemeal decisions—ones which allow developing countries to acquire the expertise and benefits that can gradually increase their bargaining power vis-à-vis MNCs.[232]

In essence, pragmatists adhere to the tenets of the "obsolescing bargaining" paradigm presented by Raymond Vernon. According to Moran, Vernon's paradigm is most effective in explaining the bargaining situation that exists between the developing

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[228] Ibid.

[229] Ibid., 113.

[230] Ibid.

[231] Ibid.

[232] Ibid.

host country and the MNC.[233] As with Schatz's notion of assertive pragmatism, risk and uncertainty play a large role in obsolescing bargaining. Due to the fact that host countries initially enter a bargaining situation with less leverage than multinationals, risk and uncertainty are most prominent when an MNC is first introduced to an economy.[234] During the initial encounter, the host country must choose between offering an over generous investment code, such as the EDA, with the hopes of receiving a few benefits or completely refusing to offer investment incentives and receiving no benefit at all. More often than not, host countries choose the former scenario.

Fortunately, as time goes on, host countries gain leverage in bargaining situations with multinationals. Once money has been sunk into a successful project, renegotiations which take place resemble what Vernon refers to as hostage situation.[235] Vernon states that MNCs cannot easily remove successful subsidiaries and this allows host countries to demand more concessions.

Host country bargaining leverage is also increased by the product life cycle theory. Carbaugh states that in the manufacturing industry goods such as electronic products pass through a trade cycle.[236] During the first two phases of the trade cycle, a company is responsible for a technological innovation in the production of a particular

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[233] Moran, 6.

[234] Ibid.

[235] Ibid.

[236] Carbaugh, 85.

good.[237] The local market is too small for mass production, but it allows the company to perfect the quality of its product and then export it to other countries with similar tastes and income levels.

As the trade cycle enters its third phase, the company finds that the success of its product demands that it relocate some of its operations overseas in order to protect export profits and decrease transportation costs.[238] Relocation is also necessary because this cost advantage does not last for long. As a company's subsidiary continues to enjoy success, technological knowledge becomes commonplace and the company's monopoly is slowly chipped away by local producers in the host country.[239] The trade cycle enters its final phase when all nations, not just the host nation, have access to the technological knowledge necessary to produce the good. The company's monopoly has now been abolished.

As evidenced in the sub-section concerning technology, the MNC makes it quite difficult for developing host nations to acquire such technology. However, "Between Dependency and Autonomy: India's Experience with the International Computer Industry" by Joseph M. Grieco asserts that India managed to reap the benefits of the product life cycle theory in the late seventies.[240] Between 1960 and 1980, the country

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[237] Ibid.

[238] Ibid.

[239] Ibid.

[240] Joseph M. Grieco, "Between Dependency and Autonomy: India's Experience with the International Computer Industry," in *Multinational Corporations: The Political*

transformed itself from an importer of technology into an inventor of technology. India accomplished this transformation by setting three goals for itself:[241]

- To participate in the ownership and control of foreign computer subsidiaries in the country.
- To have Indian producers satisfying most of the country's computer needs by the late sixties.
- To obtain access to and participate in the manufacture of the most advanced systems available internationally.

During the early sixties, India's computer industry was dominated by International Business Machines (IBM) and International Computers Limited (ICL).[242] Initially, both IBM and ICL exhibited a strong aversion to the idea of partial Indian ownership of their firms. IBM threatened to withdraw its operations from India if the country continued to make such demands.[243] ICL, which had split its production into a manufacturing sector and sales sector, chose to pacify Indian officials by offering them 40% ownership of its manufacturing sector. The sales sector was the more lucrative of the two because it was the sole distributor of the manufacturing sector's products.[244]

Despite the computer companies' aversion to sharing technology with India, the

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Economy of Foreign Direct Investment (Toronto: Lexington Books, 1985), 55.

[241] Ibid., 58.

[242] Ibid.

[243] Ibid.

[244] Ibid.

country managed to develop its own computer industry in the early seventies.[245] One of the first companies was Electronics Corporation of India Limited (ECIL).[246] By 1977, four new computer companies had emerged and India's computer industry was booming. ECIL had become the single largest systems supplier while IBM's market share collapsed. By 1980, the new firms had outpaced their predecessor (ECIL) in the production of systems. Grieco states that the following features contributed to India's success:

- The emergence of the minicomputer; these were built with increasingly powerful components which became more inexpensive over time.
- The evolution of the computer industry from the mid-sixties to the mid-seventies made technological innovations even more available to developing countries. American, Japanese and German companies toppled the British oligopoly in the computer industry giving developing countries more alternatives for minicomputers and their components.
- Between the late sixties and the early seventies, semiconductor enterprises emerged from those same countries. Computer components were their specialty. Fairchild and Motorola sold $130 million in components on the international market. [247]

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[245] Ibid., 59.

[246] Ibid.

[247] Ibid., 66-68.

These factors heightened India's bargaining power to the point where the country's Trade Development Corporation and the Atomic Energy Commission froze the operations of IBM and ICL in order to renegotiate the terms under which the companies were operating in the country.[248] As of 1980, India had Indian technology and was a viable entity in international computer circles.

India's experiences in the computer industry is what Grieco calls a "hard case" for the bargaining school. But this degree of success as far as bargaining is concerned is not the norm for the majority of developing countries, especially in the extractive sectors. In "The Renegotiation of Dependency and the Limits of State Autonomy in Mexico (1975-1982), Gary Gereffi asserts that Mexico's state owned firm (Productos Químicos Vegetales Mexicanos S.A. de C.V., a.k.a. Proquivemex) fought a losing battle in the country's barbasco industry.[249] Proquivemex was established in Mexico's attempts to nationalize the production of steroids, an industry, which was dominated by numerous multinationals. Unfortunately, due to the economy's dependence on exports, the political connections of MNCs in the Mexican government, and the fact that Proquivemex imported the technology used in production, Mexico was unable to gain any type of leverage in bargaining situations with multinationals.[250]

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[248] Ibid., 72.

[249] Gary Gereffi, "The Renegotiation of Dependency and the Limits of State Autonomy in Mexico (1975-1982)," in *Multinational Corporations: The Political Economy of Foreign Direct Investment,* ed. Theodore H. Moran (Toronto: Lexington Books, 1985), 83.

[250] Ibid., 96.

Michael Shafer presents the story of how Zambia and Zaire attempted to exert pressure on the mining companies which dominated their respective copper industries.[251] During the late seventies, the countries managed to wrest control of the mining industry from UMHK in Zaire and Zamanglo in Zambia.[252] As a show of solidarity and in the tradition of the Organization of Petrol Exporting Countries (OPEC), the two countries founded the Intergovernmental Council of Copper Exporting Countries (CIPEC). The establishment of CIPEC was not sufficient to drive multinationals out of the region. In addition to the fact that UMHK and Zamanglo had heavily guarded positions in the upper echelons of both governments, Michael Shafer outlines other obstacles that the countries encountered.

He states that one of the reasons why CIPEC as well as other nationalization efforts (Proquivemex) failed is because of a "loss of insulation."[253] MNCs such as UMHK and Zamanglo often operate in protected political and economic environments by forming powerful cartels and oligopolies that are insulated from market forces. When CIPEC nationalized the companies' holdings, they were not prepared for this loss of insulation. Amongst other factors, Zambia and Zaire had to deal with the struggle against

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[251] Michael Shafer, "Capturing the Mineral Multinationals: Advantage or Disadvantage?" in *Multinational Coroprations: The Political Economy of Foreign Direct Investment*, ed. Theodore H. Moran (Toronto: Lexington Books, 1985), 25.

[252]Ibid., 30.

[253] Ibid., 28.

white Rhodesia, chronic transportation bottlenecks, the surge in the price of oil, high international inflation rates and declining terms of trade.[254]

The failure of the pro-MNC approach to provide an accurate description of the benefits which accrue to developing host countries and the lack of bargaining power exhibited by the majority of these countries lead one to believe that developing countries are trapped in a "vicious cycle of poverty." Lewellen highlights this point when discussing the shortcomings of the economic growth theories which claim to have the answers to the development woes of lesser-developed countries (LDCs).[255] Despite the fact that developed countries have pumped billions of dollars into developing countries through trade, investment, loans and foreign aid, countries of the developing world have yet to significantly raise the standard of living for the majority of its citizens.[256] In 1990, Sierra Leone, which was home to the Hope diamond, received $35 million in foreign direct investment, $65 million in ODA and barely managed to achieve a per capita GNP of $230.[257]

Lewellen's interpretation of the vicious cycle theory is that countries remain poor because they start their development processes poor. If the majority of the citizens are

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[254] Ibid., 28-29.

[255] Lewellen, 57.

[256] Ibid.

[257] The foreign investment figure is from *Foreign Direct Investment: Lessons of Experience, Number 5* in Appendix A; the ODA and per capita GNP figures are from

too poor to save money or pay taxes, there is no money for organizations such as MNCs to borrow or for governments to create the physical infrastructure (i.e. paved roads, efficient telecommunications systems) needed to entice MNCs.[258] Lewellen goes on to state that if people are too poor to become active consumers in domestic markets, the entrepreneurial spirit in developing countries ceases to thrive.[259] Sub-Saharan Africa's economic growth and development statistics indicate that the region is caught up in this vicious cycle. The next section outlines the contemporary predicament of these countries.

The Effects of Multinationals on the Continent

The power of MNCs to keep sub-Saharan African economies dependent on them for capital, technology and employment has aided in the creation of very weak economies, which have been crippled further by a harsh international economic system. Amar Bhattacharaya, Peter J. Montiel, and Sunil Sharma, Barnet and Müller, Hazel Johnson and Julius O. Ihonvbere have all found that since the times of those early adventurers, sub-Saharan Africa has experienced macroeconomic instability, slow economic growth, rapidly decreasing domestic markets, and slow progress toward

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African Development Indicators (Washington, DC: The World Bank, 1996), 311 and 34, respectively.

[258] Lewellen, 58.

[259] Ibid.

industrialization.[260] Between 1965 and 1990, average annual growth of the region's GNP per capita (excluding Nigeria) was a mere 0.3%.[261] In 1987, 71% of sub-Saharan Africa's workforce was employed by the agricultural sector; an unbelievably high percentage for a sector whose output dropped from $51 billion in 1980 to below $34 billion in 1987.[262] Export volumes have declined by 3%, unemployment experienced a four-fold increase, and debt servicing ranged from 35% to 125%, all in the same period.[263] The average citizen has suffered as a result of these declining figures. Ihonvbere states that the annual expenditures on health care and education have declined from 26% in the early eighties to around 19% in 1988, and 34 million Africans are starving.[264]

It is almost impossible for policymakers in these countries to be concerned with the creation of what Barnet and Müller refer to as capital stock, one of the main factors reviewed when an MNC decides on a host country, when such devastation abounds.[265] Capital stock is described as, "...tangible infrastructures that enable modern societies to

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[260] Amar Bhattacharya, Peter J. Montiel, and Sunil Sharma, "Private Capital Flows to Sub-Saharan Africa: An Overview of Trends and Determinants," Research Paper for International Monetary Fund and the World Bank, 1996, 6-7.

[261] UNDP Programme/The World Bank, *African Development Indicators* (Washington, D.C.: The World Bank, 1992), 10.

[262] Hazel Johnson, 118.

[263] Ihovnbere, 301.

[264] Ibid.

[265] Barnet and Müller, 134-135.

function and to create more wealth—roads, communication systems, schools, machines and factories.[266] Unfortunately, as a result of the absence of this infrastructure, investment as a proportion of GDP has decreased from 25% in 1970 to 15.8% in 1988.[267] Furthermore, between 1991 and 1993, private capital flows were $0.3 billion annually; a decrease from $1 billion annually between 1985 and 1990.[268] Bhattacharya, Montiel, and Sharma state that this has occurred despite the fact that returns on foreign private investment have been much higher in Africa than in any other region.[269]

Small Island Developing States, Foreign Direct Investment and the Environment

Lino Bruglio's research on "Small Island Developing States and Economic Vulnerabilities" reports that even though the social and economic devastation present on the mainland of sub-Saharan Africa appears to be much more dismal than in the region's small island developing states (SIDS), these countries could also be adversely affected if this trend continues to take a downturn. The islands of Mauritius, Cape Verde, Comoros, São Tomé and Principe, the Seychelles and Madagascar are heavily dependent on foreign direct investment for their social and economic survival.[270] Omar S. Siddiqi agrees. He

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[266] Ibid., 134.

[267] Ibid., 301.

[268] William Ryrie, 198.

[269] Bhattacharya, et al, 5.

[270] Lino Bruglio, "Small Island Developing States and the Economic Vulnerabilities," *World Development* 23, no. 9 (1991): 1615-1632.

has found that in addition to lacking numerous primary resources (with the exception of Madagascar), these countries are highly constrained by transport and communication difficulties, distance from market centers and highly limited internal markets.[271] Hence, their social and economic survival depends heavily on the amount of foreign investment that flows into their economies.

The survival of SIDS is also dependent on the type of foreign investment that inhabits their economies. "Environmental Problems and Opportunities in Small Open Economies" by Naresh Singh pinpoints the fact that the focus of many island economies is on their coastal areas.[272] Solid and toxic waste management, housing and human settlements, and the determination of drinking water quality all center around the coastlines of these countries. Unfortunately, these are the areas that are threatened the most by foreign investment. According to Barnet and Cavanagh, factories are principal emitters of greenhouse gases, ozone-depleting chemicals, and toxic pollutants.[273] These realities not only threaten the viability of tourism industries, which many SIDS depend on as the main sources of foreign exchange, but they also threaten the well being of the citizens of those countries.

It is imperative that countries on the mainland of sub-Saharan Africa take note of

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[271] Ibid.; Omar S. Siddiqi, "Vulnerability and Viability of the OECS States," Symposium on the Economic Development and Prospects of the OECS States, Antigua, 10-13, June 1987.

[272] Naresh Singh, "Environmental Problems and Opportunities in Small Open Economies," Symposium of Small States, St. Kitts, March 1991.

[273] Barnet and Cavanagh, 289.

what is occurring in island economies. The Association of Small Island States (AOSIS) describes these countries as microcosms, wherein many of the problems facing the planet can be seen and dealt with in a more manageable context.[274]

These microcosms are a great asset in the effort to conquer the seemingly insurmountable environmental problems facing mainland countries. In addition to the environmental pollution committed by multinationals, E. Ike Udogu explains that warfare in countries such as Mozambique, Angola, Sudan, and Somalia has created millions of refugees.[275] The increasing amount of refugees creates environmental problems because they must encroach on scarce woodlands and fertile soil for survival.[276] The overwhelming nature of the problem forces African countries to be more concerned about daily survival of their populations and less concerned about environmental preservation.[277]

To complicate matters, multinationals and their governments are working toward alleviating themselves of environmental responsibility through intense lobbying.[278]

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[274] Available from http://www.aosis.org/letter.htm; Internet; accessed June 12, 1998.

[275] E. Ike Udogu, "The Issues of Development and Environment in Africa: An Overview," in *Sub-Saharan Africa in the 1990's: Challenges to Democracy and Development,* ed. Rukhsana A. Siddiqui (West Port, Connecticut: Praeger, 1997), 192.

[276] Ibid.

[277] Ibid., 193.

[278] Edward Goldsmith, "Global Trade and the Environment," in *The Case Against the Global Economy*, eds. Jerry Mander and Edward Goldsmith (San Fransisco: Sierra Club Books, 1996), 88.

Corporations view regulations which are used to protect the interests of labor, the poor and the environment as increasing the cost of production and reducing their competitive edge.[279] Both the Reagan and Bush administrations responded to these allegations by founding the Task Force on Regulatory Relief and the Council on Competitiveness, both of which spearheaded the campaign to relieve companies of liabilities relating to worker safety regulations, consumer product safety controls and environmental protection.[280] These movements away from environmental accountability are referred to as deregulation.[281]

Deregulation has been facilitated on a worldwide scale by the creation of free trade zones.[282] Free trade zones allow companies to operate without the constraints of labor and environmental controls. Developing countries, which are in need of foreign capital and technology and which are in fierce competition with other developing countries for foreign investment, are increasingly using these zones to attract MNCs to their economies. Goldsmith states that there are now about two hundred of these zones in the developing world and they are significantly contributing to an incredible increase in environmental devastation.[283]

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[279] Ibid.

[280] Ibid.

[281] Ibid.

[282] Ibid.

[283] Ibid.

Financing Change: The Financial Community, Eco-efficiency and Sustainable Development by Stephan Schmidheiny and Federico Zorraquín indicates that the attitudes of developing countries and MNCs concerning the environment are not congruent with sustainable development.[284] Sustainable development is defined as, "[meeting] the needs of the present without compromising the ability of future generations to meet their own needs."[285] According to Schmidheiny and Zorraquín, international business has a very important role to play in the environmental preservation of developing countries. These authors relay information about the World Business Council for Sustainable Development (WBSD): a consortium of companies that are committed to promoting eco-efficient investment in developing countries. The organization is committed to ensuring that the ecological survival of developing countries is not forgotten in excitement surrounding globalization. Some of their plans include the internalization of environmental costs and greater use of economic instruments such as taxation to procure funds for environmental cleanup.[286] Most important in the effort to protect the environment is the creation of the "green consumer" (consumers who purchase environmentally sound products).[287] Since they have had so much luck creating global consumers with pricey advertising campaigns, MNCs are in the best position to foster the development of this type of consumer.

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[284] Schmidheiny and Zorraquín, 4.

[285] Ibid.

[286] Ibid., 27.

Conclusion of Literature Review

If the proponents of foreign direct investment are correct in their assumptions surrounding the contribution of foreign capital or technology to a developing nation, then sub-Saharan Africa's social and economic indicators would not be so disheartening. Kennedy reports that about forty years ago some Asian and African countries were at the same stages in their development processes.[288] Unfortunately, many of those Asian countries have long surpassed their counterparts in Africa.

The preceding literature review indicts the MNC, the main proponent of foreign direct investment in the developing world, as, "the most salient factor in the failure to move toward international equity."[289] The ensuing research effort aims to substantiate this claim with respect to sub-Saharan Africa during two distinct periods in global economic history (1980-1989 and 1990-1995). The arguments put forth by the proponents of foreign direct investment simply are not confirmed by sub-Saharan Africa's development statistics.

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287 Ibid., 19.

288 Kennedy, 193.

289 Enloe, 26.

CHAPTER III

THEORETICAL FRAMEWORK

An economy experiences economic growth when it is able to increase its gross domestic product (GDP). GDP is defined as the total value of goods and services produced in an economy annually.[1] Every year purchases are made by consumers, companies, the government and foreigners. The sum of the spending flows of these economic actors comprises GDP, which is defined in the equation,

(3.1) $$GDP = C + I + G + (X-M)$$

where:

C = consumption of goods and services by households;
I = domestic and foreign investment in the economy; purchase of capital equipment, inventories, factories and expenditures on new housing;
G =spending on goods and services by local, state, and federal governments;
and (X-M)=net exports; the purchases of domestically produced goods by foreigners (exports) minus domestic purchases of foreign goods.

This expenditure model is only one way to define GDP. The other way is through the income model, which defines GDP as the total annual income received from the

[1] Marilu Hurt McCarty, *Dollars and Sense*, Third Edition (New York, NY: HarperCollins College Publishers, 1994), 150.

production of goods and services in an economy. In an economy, a small share of business earnings must be utilized to pay taxes and save for investment. The remaining portion must be divided among resources, which are used in production: wages, rent, interest and profit. McCarty, therefore, defines GDP as "the sum of income flows in all resource markets."[2] This model of GDP is defined in the following equation:

$$\text{GDP} = W + R + I + \pi + \text{Business Taxes and Savings} \tag{3.2}$$

where:

W = wages
R = rent
I = interest
and π = profit

The investment component of GDP is very important to lesser-developed economies that are unable to generate significant amounts of revenue from the three other types of spending. Small consumer markets, antiquated or corrupt government structures, and the low terms of trade (prices) that developing countries receive for their primary product exports, all leave investment as a primary source of income for developing countries. As evidenced in the Harrod-Domar theory, domestic investment needs to be supplemented by foreign investment in order to the obtain investment levels necessary for economic growth.

Those who subscribe to the notion of benign foreign direct investment are hard-

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[2] Ibid., 150.

pressed to offer several examples of how the foreign investment component of GDP has generated economic growth in the developing world. These proponents point to the fact that cities such as Abidjan, Lagos, and Accra can boast of five star hotels, posh residential areas, and the latest of every other type of Western convenience. However, a very important aspect of this argument is being overlooked: the way in which these luxuries are distributed within societies. No matter how much wealth is introduced into a country, it means little if resources are not distributed equitably. A case in point is the fact that citizens of developing countries are usually fighting for survival right next to futuristic skyscrapers which symbolize growth and prosperity.[3] The capital that multinationals introduce into an economy results in the division of societies, creating enclave economies that separate rather than integrate various economic sectors. The World-Systems Theory originated by Immanuel Wallerstein and updated by Volker Bornschier and Christopher Chase-Dunn best describes this phenomenon and, therefore, the effects of multinationals on developing economies.[4]

World-systems theory explains the inequality that exists within and amongst countries today from a historical viewpoint. Wallerstein describes a world-system as, "a unit with a single division of labor and multiple cultural systems."[5] This definition

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[3] Denny Braun, *The Rich Get Richer: The Rise of Income Inequality in the US and the World* (Chicago: Nelson-Hall Publishers, 1991), 130.

[4] Ibid., 30.

[5] Immanuel Wallerstein, *The Capitalist World-Economy* (Cambridge: Cambridge University Press, 1979), 5.

characterizes the nature of historical and contemporary capitalism. In the sixteenth century, the division of labor in the world economy (of which Europe was the center), was based on the utilization of free and low wage labor.[6] Different cultural systems were forced to participate in the international economic system, due to the fact that the predominance of this mode of production was primarily available in regions such as Africa, Asia and Latin America. This gave rise to a regional specialization which was reinforced by local capitalist classes who were interested in making short-run profits on their investments.[7]

Wallerstein states that this division of labor, in addition to a series of historical, ecological and geographical accidents, allowed northwestern Europe to diversify its agricultural and industrial specialization earlier than the rest of the world.[8] Northwestern Europe thus became the "core" of the world economy, specializing in the production of textiles, shipbuilding, and metal wares, all of which used wage labor as their modes of labor control.[9] Mediterranean European countries were able to obtain the status of "semi-peripheral" countries because they had the ability to produce high-cost industrial products, such as silks, and specialize in credit and specie transactions.[10] This group's

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[6] Ibid., 17.

[7] Ibid., 18.

[8] Ibid.

[9] Ibid.

[10] Ibid.

unit of labor was sharecropping.

Eastern European countries became "peripheral" by mainly exporting grains, bullion, cotton and a host of other raw materials.[11] By providing the bulk of the manpower that ran the system as well as raw materials, other peripheral countries in Africa, Asia and Latin America helped to establish the world-system as early as 1640.[12]

Due to their collective interest in the accumulation of profit, local capitalist groups in northwestern Europe began to develop strong state mechanisms which were able to take advantage of the increasingly weakened state mechanisms that existed in peripheral areas.[13] The strength of local groups in the core enabled core countries to engage in an 'unequal' exchange with peripheral countries. The majority of the wealth produced by the world-system was easily appropriated by the politically and economically stronger entities of the core countries, which offered semi-peripheral and peripheral countries low terms of trade (prices) for their primary product exports while their manufactured goods received top dollar.[14]

Wallerstein and Bornschier and Chase-Dunn acknowledge that there is room for mobility in the international system. Types of production that were growth industries for the US and several European countries, such as textiles and manufacturing, are now

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[11] Ibid.

[12] Ibid.

[13] Ibid.

[14] Ibid.

dominated by a variety of semi-peripheral and peripheral countries.[15] However, Bornschier and Chase-Dunn also note that the success of one country is usually at the expense of another, due to the fact that a division of labor amongst regions is maintained.[16]

Four factors have been singled out as having contributed to the perpetuation of this world-system. First of all, Wallerstein states that the concentration of military strength in the hands of core countries maintains stability in the system.[17] Second, he credits an ideological commitment to the system as a whole.[18] Many social classes, such as the local capitalist groups of the sixteenth century or the local bourgeoisie have always been determined to preserve the system which they believe is responsible for their well being.[19] This commitment to the preservation of the world system has led to the formation of an international bourgeoisie comprised of elite groups from the core and the periphery, whose interests allow them to identify socially and organize politically in response to market forces.[20]

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[15] Volker Bornschier and Christopher Chase-Dunn, "Stratification in the World-System," in *Transnationals and Underdevelopment* (New York: Praeger, 1985), 7.

[16] Ibid.

[17] Ibid., 22.

[18] Ibid.

[19] Ibid.

[20] Bornschier and Chase-Dunn, 3.

Furthermore, Wallerstein states that without the semi-periphery the world-system would be polarized into two very distinct and hostile entities.[21] The existence of this third category ensures that the core is not faced with a unified opposition because the semi-periphery is both the exploited and the exploiter in the world-system.[22]

According to Bornschier and Chase-Dunn, the fourth entity which perpetuates this world system is the multinational corporation.[23] These theorists state that slavery, serfdom and colonialism have been replaced by "neocolonial" forms of subjugation that are a part of the organizational structure MNCs.[24]

The presence of MNCs precludes the development of internal consumer markets which could lead to the creation of new businesses.[25] Furthermore, their political power allows them to discourage the creation of unions, which in turn keeps real wages at very low levels.[26] Lastly, the technology that MNCs introduce into an economy does nothing in terms of job creation.[27] Introducing capital-intensive technology into a labor-intensive economy causes the job market not only to stagnate, but also deteriorate. Developing

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[21] Wallerstein, 23.

[22] Ibid., 22.

[23] Bornschier and Chase-Dunn, 6.

[24] Ibid.

[25] Braun, 39.

[26] Ibid.

[27] Ibid.

countries usually have an abundance of unskilled workers who cannot participate in the technologically advanced job market that MNCs have to offer.

Bornschier and Chase-Dunn state that developing host countries are left dependent on MNCs for a variety of resources and this causes underdevelopment.[28] For instance, dependent countries develop more slowly than countries that are less dependent.[29] This dependency ensures that a country's growth potential outpaces development.[30] Lastly, countries that are dependent usually exhibit a greater degree of income inequality than less dependent countries.[31]

Braun offers several examples of income inequality in a few African countries.[32] In Côte d'Ivoire European managers make twenty times the salaries of Africans. In Swaziland the ratio is 12 to 1. Lastly, in Cameroon, three-fourths of income inequality can be attributed to the presence of White Europeans in the work force.

Max Otto Lorenz's Curve Theory graphically demonstrates the inequality that exists in these countries.[33] Graph 1 exhibits income distribution. The horizontal axis

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[28] Bornschier and Chase-Dunn, 7.

[29] Ibid.

[30] Ibid.

[31] Ibid.

[32] Braun, 100.

[33] Malcolm Gillis, Dwight H. Perkins, and Donald R. Snodgrass, *Economics of Development,* Third Edition (New York: W.W. Norton & Company, 1992), 74-77; Jan S. Hogendorn, *Economic Development*, Third Edition (New York: HarperCollins

represents the percentage of income recipients in the population and the vertical axis represents the percentage of income that they receive. The forty-five degree line in the middle represents perfect equality. For example, 40% of the population would be receiving forty percent of the income. The curved line is more indicative of reality. For example, at point A, 10% of the population receives only 1.8% of the income. The more the curve bows out, the more inequality is present in the economy. On the other hand, the closer the curve is to the 45-degree line, the more equality exists.

The Gini coefficient, which is derived from the Lorenz curve, is an easier way to assess inequality. Graph 2 indicates that if area A is divided by the Total area BCD, then one can derive a Gini coefficient. These coefficients range anywhere from 0 to 1. Countries with very unequal income distributions score between 0.50 and 0.70. Table 1 (See Appendix Two) indicates that low-income countries, especially African countries score in this range.

Bornschier and Chase-Dunn conducted a study which found that countries with high multinational penetration scores (See Table 2 in Appendix Two) have higher Gini coefficients than those with lower scores.[34] This relationship was only positive for poorer countries.[35] The exact opposite was true in developed countries. Higher multinational

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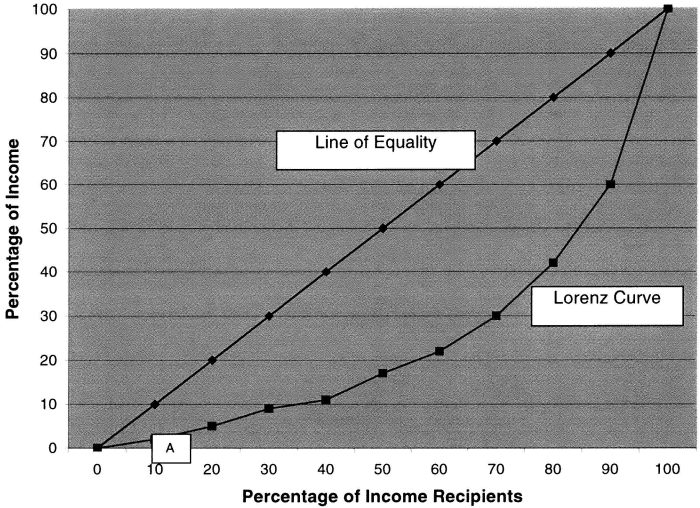
Publishers, Inc., 1996), 44-46; Michael P. Todaro, *Economic Development,* Fifth Edition (London: Longman, 1994), 135-140.

[34] Bornschier and Chase-Dunn, 125.

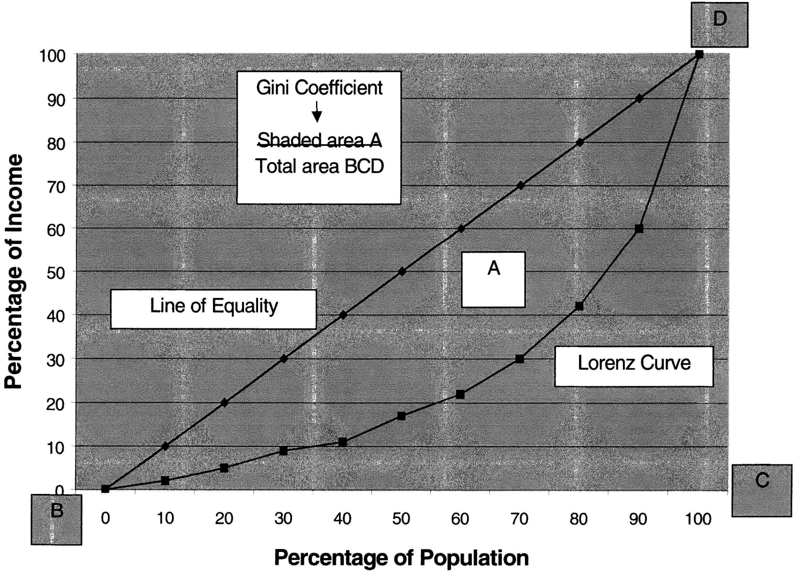
[35] Ibid.

GRAPH 1: Lorenz Curve



Source: *Economic Development,* Third Edition (New York, NY: HarperCollins College Publishers, Inc., 1996), 44.

GRAPH 2: CALCULATION OF GINI COEFFICIENT



Source: *Economics of Development,* Third Edition (New York, NY: W.W. Norton & Company, 1992), 74.

penetration was associated with lower Gini index scores.[36] This implies that there are much higher incomes in countries where multinational dominance is high. However, this income does not find its way to the rest of the population. In essence, the benefits of modernization do not "trickle down," but remain at the top. Therefore, according to the World-Systems Theory, a developing country's dilemma is two-fold. Its position in the system denies it the privilege of a level playing field. This disadvantage, in turn, makes the country less able to guarantee the survival of its population.

The purpose of this study is to investigate the effects of MNCs as principal players in the world-system on the social and economic well being of sub-Saharan African countries. The decade and a half spanning 1980-1995 marked a period during which the countries of this region were vulnerable to changes in the international economic system. Take, for instance, two of the major political and economic events during this time: the implementation of Structural Adjustment Programs (SAPs) and the fall of the Berlin Wall. Therefore, examining the impact that MNCs, which have been implicated by the world-system theory as the main proponents of the inequity that developing countries are experiencing, would enlighten scholars and professionals alike as to how the development problems in these countries can be alleviated.

This study is using two basic functional models to investigate the effects of multinationals on the sub-Saharan African region during period 1 (1980-1989) and period 2 (1990-1995). The first model represents the impact of foreign investment, foreign aid

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[36] Ibid.

and political stability on the economic growth of countries selected for the study. The second model represents the impact of foreign investment, foreign aid, and political stability on economic development. The functional equation for the first model is:

(3.1) $$EG = f(FDI, ODA, PS)$$

where:

EG = growth of a country's economy;
FDI=foreign direct investment received by countries during chosen time periods;
ODA=foreign aid received by countries during chosen time periods;
and PS =political situation in countries during chosen time periods.

This translates into the following regression equation for the first period of the study (1980-1989):

(3.2) $$EG_1 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS$$

where:

EG_1 = the average annual percentage growth in a country's gross domestic product (GDP) during period 1 (1980-1989);
FDI = real net foreign direct investment in millions of US dollars received during period 1;
ODA = real net foreign aid from all sources in millions of US dollars received during period 1;
PS = a dummy variable expressing the political situation in the country in period 1 ("1" for political stability during the period and "0" for political instability);
α_0= the intercept term (the value of EG when all independent variables are equal to zero);
α_1=the regression coefficient of FDI, or the direct effect of FDI on EG_1 when quantities of ODA and PS are held constant;
α_2 =the regression coefficient of ODA, or the direct effect of ODA on EG_1 when quantities of FDI and PS are held constant;

and α_3 =the correlation coefficient of PS; or the direct effect of PS on EG_1 when quantities of FDI and ODA are held constant.

Equation 3.1 has been slightly modified in order to study the impact of foreign direct investment, foreign aid and political stability on economic development during the same time period (period 1). The functional equation for this model is:

(3.3) $$ED = f(FDI, ODA, PS)$$

where:

ED = the level of a country's economic development during chosen time periods;
FDI=foreign direct investment received by a country during chosen time periods;
ODA=foreign aid received by a country during chosen time periods;
and PS=political situation in a country during chosen time periods.

This translates into the following regression equation for period 1:

(3.4) $$ED_1 = \alpha_0 + \alpha_1\ FDI + \alpha_2\ ODA + \alpha_3\ PS$$

where:

ED_1 = a proxy of economic development during period 1; this is measured as a country's Human Development Index (HDI) score for period 1; this measure combines quality of life components (life expectancy at birth, and literacy, mean years of schooling) with GDP adjusted for purchasing power; the lowest a country can score is "0" and the highest is "1";
FDI = real net foreign direct investment in millions of US dollars received during period 1;
ODA= real net foreign aid from all sources in millions of US dollars received during period 1;
PS = a dummy variable expressing political situation experienced in period 1 ("1" for political stability and "0" for political instability);
α_0 =the intercept term (the value of ED_1 when all independent variables equal zero);
α_1 =the regression coefficient of FDI, or the direct effect of FDI on ED_1 when quantities of ODA and PS are held constant;
α_2 =the regression coefficient of ODA, or the direct effect of ODA on ED_1 when quantities of FDI and PS are held constant;

and α_3 =the regression coefficient of PS, or the direct effect of PS on ED_1 when when quantities of FDI and ODA are held constant.

To investigate the effects of foreign direct investment, foreign aid, and political stability on economic growth during time 2, functional equation 3.1 translates into the following equation:

(3.5) $$EG_2 = \alpha_0 + \alpha_1 \, FDI + \alpha_2 \, ODA + \alpha_3 \, PS$$

where:

EG_2 = the average annual percentage growth rate in a country's GDP during period 2;
FDI =real net foreign direct investment in millions of US dollars received during period 2;
ODA =real net foreign aid from all sources in millions of US dollars received during period 2;
PS =a dummy variable expressing the political situation in countries in period 2 ("1" for political stability and "0" for political instability);
α_0 =the intercept term (the value of EG_2 when all independent variables equal zero);
α_1 =the regression coefficient of FDI, or the direct effect of FDI on EG_2 when all quantities of ODA and PS are held constant;
α_2 =the regression coefficient of ODA, or the direct effect of ODA on EG_2 when quantities of FDI and PS are held constant;
and α_3 =the regression coefficient of PS, or the direct effect of PS on EG_2 when quantities of FDI and ODA are held constant.

Finally, to examine the impact of foreign direct investment, foreign aid and political stability on economic development in period 2, functional equation 3.3 has been translated into the following regression equation:

(3.6) $$ED_2 = \alpha_0 + \alpha_1 \, FDI + \alpha_2 \, ODA + \alpha_3 \, PS$$

where:

ED_2 = a proxy of economic development in period 2, or a country's HDI score for period 2; this measure combines quality of life components (life expectancy at birth, adult literacy, mean years of schooling) with GDP adjusted for purchasing power; the lowest a country can score is 0 and the highest is 1;

FDI = real net foreign direct investment in millions of US dollars received during period 2;

ODA = real net foreign aid from all sources in millions of US dollars received during period 2;

PS =a dummy variable expressing the political situation in countries in period 2 ("1" for political stability and "0" for political instability);

α_0 =the intercept term (the value of ED_2 when all independent variables equal zero);

α_1 =the regression coefficient of FDI, or the direct effect of FDI on ED_2 when all quantities of ODA and PS are held constant;

α_2 =the regression coefficient of ODA, or the direct effect of ODA on ED_2 when all quantities of FDI and PS are held constant;

and α_3 =the regression coefficient of PS, or the direct effect of PS on ED_2 when quantities of FDI and ODA are held constant.

In all four equations the relationships between each independent variable and dependent variable are expected to be positive. Each additional \$100 of foreign direct investment is expected to bring increases in economic growth and economic development. Furthermore, a \$100 increase in foreign aid is expected to lead to an increase in economic growth and economic development. Finally, politically stable countries are expected to experience higher economic growth and development than politically unstable countries.

Chapter Four elaborates on the methodology used in the research and the sources from which the statistical data were procured.

CHAPTER IV

METHODOLOGY AND SOURCES OF DATA

Regression analysis was performed, using the SPSS for Windows computer software, to study the effects of foreign direct investment, foreign aid, and political stability on the economies of sub-Saharan African countries. The effects of these three factors on economic growth and economic development were analyzed for 30 selected countries for 1980-1989 and 1990-1995. The model used to measure the effects on economic growth during period 1 (1980-1989) was as follows:

$$EG_1 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS, \tag{4.1}$$

where:

EG_1= the average annual percentage growth rate of a country's gross domestic product (GDP) during period 1;

FDI = real net foreign direct investment in millions of US dollars received during period 1;

ODA= real net foreign aid from all sources in millions of US dollars received during period 1;

PS = a dummy variable expressing the political situation experienced in period 1("1" for political stability and 0 for political instability);

α_0 =the intercept term (the value of EG_1 when all independent variables equal zero);

α_1 =the regression coefficient of FDI, or the direct effect of FDI on EG_1 when quantities of ODA and PS are held constant;

α_2= the regression coefficient of ODA, or the direct effect of ODA on EG_1, when quantities of FDI and PS are held constant;

and α_3= the regression coefficient of PS, or the direct effect of PS on EG_1 when quantities of FDI and ODA are held constant.

In order to investigate the effects of foreign direct investment on economic development during period 1, the following model was used:

(4.2) $$ED_1 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS$$

where:

ED_1 = a proxy of economic development in period 1; a country's Human Human Development Index (HDI) score for period 1; this variable combines quality of life components (life expectancy at birth, adult literacy and Mean years of schooling) with GDP adjusted for purchasing power; the lowest a country can score is 0 and the highest is 1;

FDI = real net foreign direct investment in millions of US dollars received during period 1;

ODA = real net foreign aid from all sources in millions of US dollars received during period 1;

PS = a dummy variable expressing the political situation in countries in period 1 ("1" for political stability and "0" for political instability);

α_0 = the intercept term (the value of ED_1 when all independent variables equal zero);

α_1 = the regression coefficient of FDI, or the direct effect of FDI on ED_1 when quantities of ODA and PS are held constant;

α_2 = the regression coefficient of ODA, or the direct effect of ODA on ED_1 when quantities of FDI and PS are held constant;

and α_3 = the regression coefficient of PS, or the direct effect of PS on ED_1 when quantities of FDI and ODA are held constant.

These same models were used to study the effects of foreign direct investment, foreign aid and political stability on economic growth and economic development in period 2 (1990-1995). The model for economic growth was:

(4.3) $$EG_2 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS$$

where:

EG_2 = the average annual percentage growth rate of a country's gross domestic product (GDP) during period 2;

FDI = real net foreign direct investment in millions of US dollars received during period 2;

ODA = real net foreign aid from all sources in millions of US dollars received during period 2;

PS = a dummy variable expressing the political situation experienced in period 2 ("1" for political stability and "0" for political instability);

α_0 = the intercept term (the value of EG_2 when al independent variables equal zero);

α_1 = the regression coefficient of FDI, or the direct effect of FDI on EG_2, which is the independent impact of FDI when quantities of ODA and PS are held constant;

α_2 = the regression coefficient of ODA, or the direct effect of ODA on EG_2, which is the independent impact of ODA when quantities of FDI and PS are held constant;

and α_3 = the regression coefficient of PS, or the direct effect of PS on EG_2, which is the independent impact of PS when quantities of FDI and ODA are held constant.

Finally, the impact of foreign direct investment, foreign aid and political stability on economic growth was measured with this equation:

$$ED_2 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS \tag{4.4}$$

where:

ED_2 = a proxy of economic development in period 2; or a country's Human Development Index (HDI) score during 2; this measure combines quality of life Components (life expectancy at birth, adult literacy and mean years of schooling) with GDP adjusted for purchasing power; the lowest a can score is 0 and the highest is 1;

FDI = real net foreign direct investment in millions of US dollars received during period 2;

ODA = real net foreign aid from all sources in millions of US dollars received during period 2;

PS = a dummy variable expressing the political situation in countries in period 2 ("1" for political stability and "0" for being political instability);

α_0 = the intercept term; (the value of ED_2 when all independent variables equal zero);

α_1 = the regression coefficient of FDI, or the direct effect of FDI on economic development during period 2 (ED_2);

α_2 = the regression coefficient of ODA, or the direct effect of ODA on economic development during period 2 (ED_2);

and α_3 = the regression coefficient of PS, or the direct effect of PS on economic development during period 2 (ED_2).

The relationships between all variables in these equations are expected to be positive. For each additional dollar of foreign investment, economic growth and development are expected to increase. For each additional dollar of foreign aid, economic growth and development are expected to increase. And, lastly, economic growth and development are expected to increase in countries that were politically stable, as opposed to those that were unstable.

The search for statistical data on sub-Saharan Africa proved to be quite tedious in that time series data on social and economic statistics for sub-Saharan Africa are difficult to obtain. This is reflected in the number and types of sources used to gather data for this thesis. Gross domestic product figures were collected from *World Development Indicators,* 1997 and 1998. Due to the fact that the earliest Human Development Index (HDI) scores are found in the late eighties, this study used the HDI scores for 1990 to represent economic development in period 1 (1980-1989) and HDI scores for 1994 to represent economic development in period 2 (1990-1995). HDI scores were procured from two editions of the *Human Development Report*, 1993 and 1997.

FDI in millions of US dollars was averaged from time series data provided by *Foreign Direct Investment: Lessons of Experience, Number 5*, 1997 and *African Development Indicators*, 1995. ODA in millions of US dollars was also averaged from time series data provided by *African Development Indicators*, 1995 and 1997. The ODA that South Africa received in period 1 was averaged from time series data in the 1994 edition of *World Tables*.

The FDI figures for period 1, which were obtained from *African Development Indicators, 1995* and the ODA figures for period 1 were only available in 1994 dollars.

The consumer price index (CPI) was used to convert them into 1996 dollars. The 1996 CPI was found in the *Statistical Abstract of the United States, 1997.*

Finally, information on Political Stability was obtained *from The Political Handbook of the World,* 1997. This source contains detailed summaries of the political situation in almost every country in the world from the 1950's to January 15, 1996.

The results of this research are discussed in Chapter Five: Empirical Analysis.

CHAPTER V

EMPIRICAL ANALYSIS

Four regression analyses were performed to investigate the effects of foreign direct investment on the economic growth and development of sub-Saharan African countries during the periods, 1980-1989 and 1990-1995. The first sought to measure the impact of foreign direct investment (FDI), foreign aid (ODA), and political stability (PS) on economic growth in period one (1980-1989), using the equation:

$$EG_1 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS \tag{5.1}$$

The results of this regression are as follows:

$$\begin{array}{lcccc} EG_1 = & 3.232 & - .0016\ FDI & - .0027\ ODA & - .120\ PS \\ & (1.005) & (.005) & (.004) & (.922) \\ t = & (3.217) & (-.315) & (-.664) & (-.131) \\ & R^2 = -.094 & & F = .172 & \end{array} \tag{5.2}$$

Figures in the first set of parentheses are standard error values.

The impact of foreign direct investment, foreign aid and political stability on economic development during period 1 (1980-1989) was measured using this equation:

$$ED_1 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS \tag{5.3}$$

This equation yielded the following results:

(5.4) $$ED_1 = .254 - .000067\ FDI - .00044\ ODA + .143\ PS$$
$$\quad\ (.073) \quad (.000) \qquad (.000) \quad (.067)$$

$$t = (3.48) \quad (-.186) \qquad (-1.495) \quad (2.145)$$

$$R^2 = .130 \qquad\qquad F = 2.445$$

Figures in the first set of parentheses are standard error values.

In period 2 (1990-1995), the effects of foreign direct investment, foreign aid and political stability on economic growth were measured with the following equation:

(5.5) $$EG_2 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS$$

The output for this regression is:

(5.6) $$EG_2 = .556 + .00197\ FDI + .000494\ ODA + 2.52\ PS$$
$$\quad (.886) \quad (.002) \qquad (.002) \quad (1.07)$$

$$t = (.628) \quad (.818) \qquad (.320) \quad (2.357)$$

$$R^2 = .105 \qquad\qquad F = 2.135$$

Figures in the first set of parentheses are standard error values.

The impact of foreign direct investment, foreign aid and political stability on economic development during period 2 was measured using this equation:

(5.7) $$ED_2 = \alpha_0 + \alpha_1 FDI + \alpha_2 ODA + \alpha_3 PS$$

The effects of these variables on economic development in period 2 are expressed in the following results:

(5.8) $$ED_2 = .423 - .0000129\ FDI - .000189\ ODA + .171\ PS$$
$$(.040) \quad (.000) \qquad (.000) \quad (.331)$$

$$t = (10.68) \quad (-.119) \qquad (-2.716) \quad (3.559)$$

$R^2 = .331$ $F = 5.77$

Figures in first set of parentheses are standard error values.

Analysis of Results

At the onset of the regression analysis, positive relationships were expected between each independent variable (foreign direct investment, foreign aid, political stability) and the dependent variable (economic growth). The outcome of the analysis for period 1 proved otherwise. The results of equation 5.1 reveal a negative, and insignificant relationship between each independent variable and economic growth in period 1. The regression coefficient for FDI (-.0016) demonstrates that, holding foreign aid (ODA) and political stability (PS) constant, every $100 dollar increase in foreign direct investment (FDI) is associated with a .16% decrease in gross domestic product (GDP). The t-statistic (-.315) indicates that this relationship is highly insignificant and is only applicable to 25% of the countries studied (significance of t is .755).

The relationship between foreign aid (ODA) and economic growth resembles that of foreign direct investment and economic growth. Holding foreign direct investment (FDI) and political stability (PS) constant, the regression coefficient (-.0027) reveals that every $100 dollar increase in foreign aid (ODA) leads to a .27% decrease in economic growth. The t-statistic of this relationship is lower than those for the other two relationships in the equation at -.664. The low t-value renders this relationship insignificant.

The relationship between economic growth and political stability was also surprisingly negative. Holding foreign direct investment (FDI) and foreign aid (ODA) constant, politically stable countries experienced a .12% decrease in economic growth during period one. Again, this relationship was found to be insignificant, with a t-value of -.131. Also, this result was only applicable to 10% of the countries used in the study (significance of t is .897).

The adjusted R^2 figure indicates that only -.094% of the variation in the dependent variable is accounted for by the independent variables. The F-statistic (.172) reveals a highly insignificant regression equation.

A positive relationship was also expected between each independent variable (foreign direct investment, foreign aid, and political stability) and the dependent variable (economic development). The outcome of regression equation 5.3 partially met expectations. The regression coefficient for FDI (-.000067) reveals that for every $100 dollar increase in foreign direct investment (FDI) a country experiences a .0067 decrease in its HDI score. This relationship actually has also has a negative t-value, and its significance level reveals that this relationship applies to only 15% of the countries studied (significance of t is .854).

According to the regression coefficient for ODA (-.000441), holding foreign investment (FDI) and political stability (PS) constant, every $100 dollar increase in foreign aid is accompanied by a .0441 decrease in a country's HDI score. Even though the relationship has a negative t-value (t = -1.495), it was found in 85% of the countries studied (significance of t is .147). The significance level demonstrates that the relationship is insignificant.

Political stability and economic development had a positive relationship in period 1. Holding foreign direct investment (FDI) and foreign aid (ODA) constant, politically stable countries had higher HDI scores. They were higher by .143. This relationship was stronger than all others so far, with a t-value of 2.145, which rendered the variable significant at the 4% level.

The adjusted R^2 reveals that 13% of the variation in economic growth can be accounted for by foreign direct investment (FDI), foreign aid (ODA) and political stability (PS). The F-statistic of 2.445 was significant, indicating a strong regression equation.

Even though the significance of the relationships in Equation 5.5 varied, all were consistent with model expectations. The relationships between each independent variable (foreign direct investment, foreign aid, and political stability) and the dependent variable (economic growth) were all positive. The regression coefficient for FDI indicates that for every $100 dollar increase in foreign investment, economic growth increases by .0197%. This relationship is insignificant due to the low significance of its t-value (.818). This relationship occurred in only 58% of the countries used in this study.

The regression coefficient for ODA demonstrates that an increase in foreign aid is also accompanied by an increase in economic growth. Holding FDI and PS constant, for every $100 increase in foreign aid (ODA), economic growth increases by .0494%. However, this relationship is insignificant as reflected in its low t-value of .320.

According to the results in Equation 5.5, countries that were politically stable during period 2 experienced economic growth rates that were 2.52 percentage points higher than countries that were unstable. This relationship was found to be highly significant at the 3% level.

The adjusted R^2 for the equation indicates that only 11% of the variation in the dependent variable (economic growth) is accounted for by the independent variables. Unfortunately, the regression as a whole falls just short of significance at a 12% level of probability.

Equation 5.7 yielded some very interesting results. Holding foreign aid (ODA) and political stability (PS) constant, every additional $100 of foreign direct investment (FDI) led to a .00129 decrease in a country's Human Development Index score. With a t-value of -.119, these results applied to only 9% of the countries studied.

The regression coefficient for ODA indicates a similar relationship. For every $100 increase in ODA, the Human Development Index (HDI) decreases by .0189. The t-value (-2.716) has a significance value of 2%, which indicates that the results apply to 98% of the countries used in the study.

Surprisingly, the relationship between political stability and economic development was the most significant in this regression. Countries that were stable during period 2 achieved higher HDI scores than countries that were unstable. The Human Development Index (HDI) of politically stable countries was higher than politically unstable countries by .171. The t-value (3.559) implies that this relationship is highly significant at the 1% level, which means that it applies to 99% of the countries used in the study.

The adjusted R^2 indicates that 33% of the variation in the dependent variable is accounted for by the independent variables. These are strong results, as is the F-statistic of 5.774, which indicates that the regression as a whole is significant at a 1% significance level.

The mixed results of these regressions warranted remedial work on the model to control for multicollinearity and to examine the individual effects of each independent variable.

To investigate the individual impact of foreign direct investment on economic growth during period 1, the following regression was performed:

(5.9) $$EG_1 = \alpha_0 + \alpha_1 \text{ FDI}$$

The effect of foreign investment on economic growth during this period is as follows:

(5.10) $$\underset{(.440)}{EG_1 = 2.707} + \underset{(.005)}{.0012 \text{ FDI}}$$

$$t = (6.159) \quad (-.252)$$

$$R^2 = -.033 \quad F = .064$$

Figures in parentheses are standard error measures.

The impact of foreign aid on economic growth during period 1 was tested with a similar equation:

(5.11) $$EG_1 = \alpha_0 + \alpha_2 ODA$$

The results are the following:

(5.12) $$EG_1 = 3.056 + .00244\ ODA$$
$$(.740) \quad (.004)$$

$$t = (4.129) \quad (-.630)$$

$$R^2 = -.021 \quad F = .397$$

Figures in parentheses are standard error values.

The impact of political instability on economic growth during period 1 was obtained from this equation:

(5.13) $$EG_1 = \alpha_0 + \alpha_3\ PS$$

This equation yielded the following results:

(5.14) $$EG_1 = 2.77 - .155\ PS$$
$$(.710) \quad (.870)$$

$$t = (3.901) \quad (-.178)$$

$$R^2 = -.035 \quad F = .032$$

Figures in parentheses are standard error values.

The impact of foreign direct investment on economic development during period 1 was analyzed using this equation:

(5.15) $$ED_1 = \alpha_0 + \alpha_1 FDI$$

The results are as follows:

(5.16) $$ED_1 = .269 + .00021 \text{ FDI}$$
$$(.036) \quad (.000)$$

$$t = (7.57) \quad (.558)$$

$$R^2 = -.024 \quad F = .311$$

Figures in parentheses are standard error terms.

The effect of foreign aid on economic development during period 1 was measured using the following regression equation:

(5.17) $$ED_1 = \alpha_0 + \alpha_2 \text{ ODA}$$

The results are as follows:

(5.18) $$ED_1 = .352 + .00047 \text{ ODA}$$
$$(.058) \quad (.000)$$

$$t = (6.05) \quad (-1.55)$$

$$R^2 = .046 \quad F = 2.394$$

Figures in parentheses are standard error terms.

The direct effect of political stability on economic development during period 1 was measured with this regression equation:

(5.19) $$ED_1 = \alpha_0 + \alpha_3 PS$$

The results of this regression run are:

(5.20) $$ED_1 = .179 + .146\ PS$$
$$\quad (.053) \quad (.065)$$

$$t = (3.37) \quad (2.25)$$

$$R^2 = .123 \quad F = 5.053$$

Figures in parentheses are standard error terms.

The impact of foreign direct investment in period 2 was measured by the following equation:

(5.21) $$EG_2 = \alpha_0 + \alpha_1 FDI$$

The results of this regression are:

(5.22) $$EG_2 = 1.743 + .000992\ FDI$$
$$\quad (.540) \quad (.003)$$

$$t = (3.23) \quad (.359)$$

$$R^2 = -.031 \quad F = .129$$

Figures in parentheses are standard error terms.

The effect of foreign aid on economic growth during period 2 was deduced from this equation:

(5.23) $$EG_2 = \alpha_0 + \alpha_2\ ODA$$

This equation yielded the following results:

(5.24) $$EG_2 = 1.21 + .0013\ ODA$$
$$(.895) \quad (.002)$$

$$t = (1.352) \quad (.786)$$

$$R^2 = -.013 \quad F = .618$$

Figures in parentheses are standard error values.

The direct impact of political stability on economic growth during period 2 was measured using the following regression equation:

(5.25) $$EG_2 = \alpha_0 + \alpha_3\ PS$$

The results were as follows:

(5.26) $$EG_2 = .887 + 2.431\ PS$$
$$(.608) \quad (1.003)$$

$$t = (1.46) \quad (2.422)$$

$$R^2 = .144 \quad F = 5.868$$

Figures in parentheses are standard error terms.

The impact on economic development in period 2 was measured using the following equation:

(5.27) $$ED_2 = \alpha_0 + \alpha_1\ FDI$$

This regression equation yielded the following results:

(5.28) $$ED_2 = .403 + .000084\ FDI$$
$$(.028) \quad (.000)$$

$$t = (14.426) \ (-.637)$$

$$R^2 = .014 \ F = .406$$

Figures in parentheses are standard error values.

This equation was used to measure the direct impact of foreign aid on economic development during period 2:

(5.29) $$ED_2 = \alpha_0 + \alpha_2\ ODA$$

The regression yielded the following results:

(5.30) $$ED_2 = .462 + .00014\ ODA$$
$$(.045) \quad (.000)$$

$$t = (10.291) \quad (-1.693)$$

$$R^2 = .061 \quad F = 2.868$$

Figures in parentheses are standard error values.

Finally, the effect of political stability on economic development during period 2, was measured using this equation:

(5.31) $$ED_2 = \alpha_0 + \alpha_3\ PS$$

The results were as follows:

(5.32) $$ED_2 = .347 + .145PS$$
$$(.031) \quad (.050)$$

$$t = (11.353)(2.879)$$

$$R^2 = .201 \quad F = 8.290$$

Figures in parentheses are standard error values.

Analysis of Revised Regression Models

As evidenced by the significance of the t- and F-statistics, the relationships between foreign direct investment and economic growth and development remained insignificant in both time periods. The relationship between foreign aid and economic growth in both time periods and the relationship between foreign aid and economic development in period 1 also remained insignificant. Surprisingly, the highly significant relationship, which occurred between foreign aid and economic development in period 2 (Equation 5.7), was found to be insignificant in the revised regression model (Equation 5.29).

The results of the regressions using political stability as the independent variable varied. Equation 5.13 did not show a significant relationship between political stability and economic growth during period 1. During period 2, however, the relationship between political stability and economic growth was highly significant. According to Equation 5.25, countries that were politically stable during period 2 experienced a 2.43% increase in economic growth. This relationship was found to be significant at the 2% significance level.

Political stability's effect on economic development during both time periods was just as dynamic. Equation 5.19 reveals that politically stable countries had Human Development Index (HDI) scores that were .146 higher than politically unstable countries. The adjusted R^2 for the equation indicates that 12% of the variation in economic development is accounted for by political stability, and both t- and F-statistics found the relationship between the two variables to be highly significant at the 3% level.

Political stability and economic development exhibited a stronger relationship during period 2. In Equation 5.31, the regression coefficient is slightly lower at .145 than the one in Equation 5.8, which was .171, but its level of significance is higher. According to the adjusted R^2 for this equation, political stability is responsible for 20% of the variation in the Human Development Index (HDI). Both t- and F-statistics indicate this variable be significant at the1% level.

Summary of Results

Except for the insignificant relationship between political stability and economic growth during period 1, political stability produced expected results with respect to economic growth and economic development. The fact that politically stable countries experienced growth rates that were 2.43% higher than the growth rates of unstable countries during period 2 says quite a bit about the growth potential of sub-Saharan African countries. A growth rate of 2.43% is impressive, especially when compared to the growth rates of developed countries. Take the United States, for instance. During period 2, the average annual percentage growth rate of the economy was 2.6%.[1]

As far as economic development is concerned, it is quite logical that politically stable countries would have higher economic development scores than politically unstable countries. More often than not, politically stable countries have the time and the resources to devote themselves to the improvement of the quality of life of their populations.

The effects that political stability had on economic growth and economic development are consistent with the findings of Kwabena Gyimah-Brempong and Thomas L. Traynor, which state that political instability prohibits a country's ability to save and accumulate capital, which in turn, reduces a country's opportunity to experience economic growth and development.[2]

The results of the regressions, which used foreign investment and foreign aid as independent variables, were inconclusive. They are inconsistent with other empirical findings and in direct contrast with the tenets of the theoretical framework used for this research, even when the variables were analyzed individually.

The impact of foreign direct investment, which has been known to affect economic growth positively and negatively in developing countries, was not significant in either time period.[3] What is more surprising is that foreign direct investment, which

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[1] World Bank, *World Development Indicators, 1997* (Washington, DC: International Bank for Reconstruction and Development/The World Bank), 132.

[2] Kwabena Gyimah-Brempong and Thomas L. Traynor, "Political Instability and Savings in Less Developed Countries," *Journal of Development Studies* 32, no. 5 (June 1996): 695.

reportedly has a negative impact on development in various developing countries, appeared to have no significant effect on economic development in either time period.[4]

Foreign aid was expected to have a positive effect on economic growth and development, but the results of the regression runs did not find this effect. According to Ismail Seregaldin, those who support the continued flow of foreign aid to developing countries claim that countries which received aid from Organization for Economic Cooperation and Development (OECD) countries had higher per capita growth rates than the donor countries themselves between 1953 and 1988.[5] He also relays the fact that these proponents state that countries which receive aid from OECD countries are improving their quality of life indicators faster than the donor countries did.[6]

The insignificant relationships between foreign aid and economic growth and economic development probably stem from the fact that the aid which developing countries receive is usually not distributed to the groups of society which will benefit the most from it. The 1992 *Human Development Report* claims that foreign aid suffers from

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[3] Agbeko Katapu, "Economic Success: Ivory Coast and Kenya," in *Workable Strategies to End Africa's Poverty: Some Aspects of Nation Management Economics* (Syracuse, New York: Center for Management Economics, 1986), 54; Volker Bornschier and Christopher Chase-Dunn, "Stratification in the World-System," in *Transnational Corporations and Underdevelopment* (New York: Praeger, 1985), 3.

[4] Denny Braun, *The Rich Get Richer: The Rise of Income Inequality in the US and the World* (Chicago: Nelson-Hall Publishers, 1991), 131.

[5] Ismail Serageldin, "Foreign Aid and Economic Development," in *Development Partners: Aid and Cooperation in the 1990's* (United States of America: Swedish International Development Authority, 1993), 8-9.

[6] Ibid., 9.

several critical weaknesses.[7] First and foremost, it is disproportionately distributed among developing regions.[8] Ten of the countries that are home to 75% of the world's population only receive 25% of aid to developing countries.[9] Second, the allocation of aid is not determined by basic need, but by the whims of the political systems in donor countries.[10] Lastly, the foreign aid system is a flat rate system of voluntary taxation whose target is 0.7% for all donor countries, regardless of the size of their respective GNPs.[11] This has probably contributed to the fact that developed countries do not donate enough to developing countries.[12] Serageldin implicates the actions of developing country rulers as one of the main reasons why developing countries do not benefit from aid.[13] He quotes two researchers who state that aid does not reach the poor because it is given to rulers whose public spending habits are governed by their personal or political agendas; agendas which most likely do not consider the needs of the poor a priority.[14]

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[7] United Nations Development Programme, *Human Development Report, 1992* (New York: Oxford University Press, 1992), 44.

[8] Ibid.

[9] Ibid.

[10] Ibid., 45.

[11] Ibid.

[12] Ibid.

[13] Serageldin, 11

[14] Ibid., 11.

Despite the fact that the results concerning foreign investment contrasted with expected results, they are consistent with the realities facing sub-Saharan African countries. Bhattacharya et al. state that international private capital flows to sub-Saharan Africa as a percentage of GDP are lower than any other developing region, except for the Middle East and North Africa.[15] William Ryrie reports that between 1985 and 1990, sub-Saharan Africa only received 1% of all private capital flows to the developing world.[16] From 1991 to 1993 this figure dropped to .3%.[17] The region did experience an increase in investment from OECD countries between 1989 and 1995, but it was only concentrated in sub-Saharan Africa's three oil-exporting countries: Congo, Gabon and Nigeria.[18]

Even though this study only pinpointed three variables which can be held accountable for sub-Saharan Africa's economic growth and development performance, it by no means ignores the reality that other factors have probably had a more significant effect on Africa's growth and development. For instance, trade flows have been a major source of foreign exchange for sub-Saharan African countries which were forced to assume the role of primary product export economies for decades and therefore may have had more of an impact on economic growth and development than the factors used in the

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[15] Bhattacharya et al., 2.

[16] William Ryrie, *First World, Third World* (London: MacMillan Press Ltd., 1995), 198.

[17] Ibid.

[18] Paul Bennell, "Foreign Direct Investment in Africa: Rhetoric and Reality,"

study. Also, the seventies oil crisis and the ensuing Structural Adjustment Programs (SAPs) had devastating effects on many sub-Saharan African countries. Not only did both occurrences gear African economies toward the repayment of overwhelming debt, but at the same time, they also reduced the amount of capital that government's were permitted to spend on social services.[19] In adjusted countries in Africa, per capita government spending decreased from 1980 to 1987.[20] During the same time period, the share of government spending on interest payments increased from 7.7% to 12.5%.[21]

The importance of these factors to an explanation of sub-Saharan Africa's development woes by no means rules out foreign direct investment as one of many possible solutions to the region's development-related problems. One of the primary goals of the National Summit on Africa, which convened during May 6-10, 1998 in Atlanta, Georgia, was to increase foreign direct investment to sub-Saharan Africa. This is actually one of the objectives of President Bill Clinton's proposed African Growth and Opportunity Act. As a participant in the Summit, and the Economic Development, Trade and Investment and Job Creation roundtable in particular, the researcher was able to listen in on suggestions for bringing about this particular situation. Someone suggested that the US government promote the development of micro- and small enterprises, which

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SAIS Review 17, no. 2 (1997): 131.

[19] David C. Korten, *When Corporations Rule the World* (West Hartford, Connecticut: Kumarian Press, Inc., 1995), 164.

[20] Ibid.

[21] Ibid.

have been known to efficiently utilize the productive assets of developing countries.[22] Another suggested the introduction of more American banks into African economies to ensure a source of foreign exchange for American investors. Lastly, a participant suggested that the American government offer guarantees for American investment in Africa. Overall, it was agreed that Africa needs a "Marshall Plan" similar to the one given to European countries after the Second World War. The next summit, which convenes in Washington, DC next year, will hopefully announce that some progress has been made in this direction.

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[22] Louis T. Wells, Jr. "Small-Scale Manufacturing as a Competitive Advantage," in *Multinational Corporations: The Political Economy of Foreign Direct Investment,* ed. Theodore H. Moran (Toronto: Lexington Books, 1985), 119.

CHAPTER VI

CONCLUSIONS

So far, the nineties have been very enlightening. It is a decade that will be reflected on as the heyday of globalization—the finest hour of capital accumulation on an international scale. However, with this cause for celebration comes a word of warning: even success of this magnitude has a price, and this price is being paid by the millions of disadvantaged citizens of the developing world. As billions of dollars are being traded by multinationals everyday, large portions of the populations in the developing world are struggling to survive.

This study provided a bit of insight into the cause of such disparity. In the eighties and early nineties, there were several sub-Saharan African countries that could claim to be experiencing political stability. This variable yielded positive and significant effects on economic growth and development. Political instability can therefore be pinpointed as one of the main causes of human suffering in the region.

Regression results concerning the effects of foreign direct investment and foreign aid were inconsistent with expected results that speculated that foreign direct investment and foreign aid would have positive and significant effects on economic growth and development. However, these results also offer insights into the social and economic dilemmas facing sub-Saharan African countries. Even after the end of the Cold War, the region has not been able to acquire its fair share of foreign direct investment. And, despite large foreign aid flows, the region has yet to fully benefit from the injection of foreign capital into its economies.

Even though globalization has brought about impressive economic achievements, the social dimension of globalization leaves a lot to be desired. As the millenium draws to a close, it is imperative that the international economic community as a whole formally address the marginalization of sub-Saharan African countries, in order to achieve a higher quality of life for one of the world's most populous regions.

APPENDIX 1

THIRTY COUNTRIES USED IN STUDY

Benin
Botswana
Burkina Faso
Cameroon
Central African Republic
Chad
Democratic Republic of Congo
People's Republic of Congo
Côte d'Ivoire
Ethiopia
Gabon
Ghana
Kenya
Lesotho
Madagascar
Malawi
Mauritania
Mauritius
Mozambique
Niger
Nigeria
Senegal
Sierra Leone
South Africa
Tanzania
Togo
Uganda
Zambia
Zimbabwe

APPENDIX 2

TABLE 1

GINI COEFFICIENT, 1975-1993

Ecuador	0.66	Hong Kong	0.45
Jamaica	0.66	Sri Lanka	0.45
Honduras	0.62	Philippines	0.45
Sierra Leone	0.59	Costa Rica	0.42
Brazil	0.57	Singapore	0.42
Panama	0.57	India	0.42
Côte d'Ivoire	0.55	El Salvador	0.40
Nepal	0.53	Tunisia	0.40
Turkey	0.51	Bangladesh	0.39
Mexico	0.50	Egypt	0.38
Malaysia	0.48	United States	0.38
Thailand	0.47	South Korea	0.36
Chile	0.46	Pakistan	0.36
Iran	0.46	Peru	0.31
Colombia	0.45	Indonesia	0.31

Source: *Economic Development*, Third Edition (New York, NY: HarperCollins College Publishers, Inc., 1996), 47.

TABLE 2

MULTINATIONAL PENETRATION OF COUNTRIES BY POSITION WITHIN THE MODERN WORLD SYSTEM: 1967

Core	Semi-Periphery	Periphery	
Australia (101)	Argentina (61.4)	Afghanistan (3.3)	Laos (NA)
Austria (23.8)	Bulgaria (NA)	Albania (NA)	Liberia (103)
Belgium (52.2)	Burma (1.3)	Algeria (77.5)	Libya (104)
Canada (104.0)	Cuba (NA)	Benin (21.1)	Madagascar (31.8)
Denmark (72.1)	Cyprus (NA)	Bolivia (60.5)	Mali (5.0)
France (30.1)	E. Germany (NA)	Brazil (67.1)	Malta (NA)
Greece (27.8)	Finland (10.9)	Burkina Faso (14.0)	Mauritania (102)
Italy (31.6)	Hungary (NA)	Burundi (22.8)	Mexico (43.5)
Japan (3.1)	India (6.6)	Cameroon (60.6)	Mongolia (NA)
Luxembourg (NA)	Iran (44.5)	Cent. Afri. Rep.(48.9)	Morocco (25.5)
Netherlands (40.0)	Ireland (102)	Chad (17.3)	Nepal (3.9)
Norway (24.3)	Israel (26.5)	Chile (101)	New Zealand (64.8)
Sweden (18.9)	Jordan (21.9)	China (NA)	Nicaragua (58.0)
Switzerland (36.8)	Kenya (34.4)	Colombia (52.1)	Niger (20.7)
U.K. (64.8)	Lebanon (NA)	Congo (NA)	Nigeria (58.5)
U.S.A. (18.0)	Malaysia (100)	Costa Rica (94.1)	Panama (105)
W. Germany (27.7)	Pakistan (21.6)	Czechoslovakia (NA)	Paraguay (29.0)
Yugoslavia (0)	Peru (78.8)	Dominican Rep. (61.2)	Poland (NA)
	Philippines (38.9)	Ecuador (26.0)	Rwanda (22.4)
	Portugal (53.6)	Egypt (3.9)	Saudi Arabia (102)
	Rumania (0)	El Salvador (42.4)	Senegal (90.1)
	S. Africa (101)	Ethiopia (10.2)	Sierra Leone (85.5)
	S. Korea (5.9)	Gabon (NA)	Somalia (18.0)
	Spain (36.4)	Ghana (55.4)	Sudan (7.8)
	Sri Lanka (42.8)	Guatemala (51.8)	Syria (9.9)
	Turkey (11.5)	Guinea (83.0)	Taiwan (NA)
	Uruguay (21.0)	Haiti (46.2)	Thailand (13.7)
	U.S.S.R. (NA)	Honduras (101)	Togo (60.9)
	Venezuela (103)	Iceland (NA)	Trinidad and Tobago (105)
		Indonesia (7.3)	
		Iraq (31.9)	Tunisia (48.6)
		Ivory Coast (85.5)	Uganda (14.4)
		Jamaica (104)	Vietnam (NA)
		Kampuchea (NA)	Yemen (NA)
		Kuwait (NA)	Zaire (60.0)
(NA = Not Available)		Average = 60	

Source: *The Rich Get Richer: The Rise of Income Inequality in the United States and the World* (Chicago: Nelson-Hall Publishers, 1991), 117.

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